

**THE NEWS CORPORATION/DIRECTV DEAL: THE  
MARRIAGE OF CONTENT AND GLOBAL DIS-  
TRIBUTION**

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**HEARING**

BEFORE THE  
SUBCOMMITTEE ON ANTITRUST,  
COMPETITION POLICY AND CONSUMER RIGHTS  
OF THE  
COMMITTEE ON THE JUDICIARY  
UNITED STATES SENATE  
ONE HUNDRED EIGHTH CONGRESS

FIRST SESSION

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## **THE NEWS CORPORATION/DIRECTV DEAL: THE MARRIAGE OF CONTENT AND GLOBAL DISTRIBUTION**

WEDNESDAY, JUNE 18, 2003

UNITED STATES SENATE,  
SUBCOMMITTEE ON ANTITRUST, COMPETITION POLICY, AND  
CONSUMER RIGHTS, OF THE COMMITTEE ON THE JUDICIARY,  
*Washington, DC.*

The Subcommittee met, pursuant to notice, at 2:37 p.m., in room SD-226, Dirksen Senate Office Building, Hon. Mike DeWine, Chairman of the Subcommittee, presiding.

Present: Senators DeWine, Specter, Kohl, and Leahy.

### **OPENING STATEMENT OF HON. MIKE DEWINE, A U.S. SENATOR FROM THE STATE OF OHIO**

Chairman DEWINE. Well, good afternoon and welcome to the Antitrust Subcommittee hearing on the proposed transaction between News Corporation and DIRECTV.

Just 15 months ago, this Subcommittee held a hearing to examine another deal involving DIRECTV, the proposed merger between EchoStar and DIRECTV. Many had expressed alarm about that proposed merger, and ultimately the Justice Department and the FCC moved to block the deal.

The News Corporation/DIRECTV deal we are examining today is fundamentally different, of course, from the merger that we examined 15 months ago. Unlike the prior deal, this one does not involve two companies that are direct competitors. Instead, News Corporation and DIRECTV compete in different markets.

The United States, News Corporation competes primarily as a programmer, owning such properties as the Fox Network and cable networks, such as Fox News Channel and numerous regional sports networks. As a result of this ownership, News Corporation provides some of the most popular programming in the United States.

DIRECTV competes as a distributor of multichannel video programming, providing direct satellite service to over 11 million subscribers. DIRECTV carries News Corporation programming, and other programming, to subscribers. Thus, this deal is a vertical deal, involving a combination between a supplier of programming, News Corporation, and a distributor of programming, DIRECTV.

Vertical combinations, like this one, can potentially create efficiencies for the combining parties and benefits for consumers.

Vertical deals also, however, can raise competitive concerns, though typically fewer and different kinds of concerns than those raised by deals between direct “horizontal” competitors. Deals such as this one may also raise policy concerns that do go beyond anti-trust issues.

In our hearing today, we will explore both the potential efficiencies and benefits of News Corporation’s combination with DIRECTV and the concerns that the deal raises.

News Corporation and DIRECTV argue that numerous benefits will flow from their merger. News Corporation will bring its years of experience as a satellite operator in other countries and its record as an aggressive, innovative competitor to the American video marketplace.

For example, in other countries, News Corporation—or News Corp—has introduced several interactive features, such as interactive shopping and interactive games with its satellite services.

If, in fact, News Corp is successful in strengthening the competitive offerings of DIRECTV, that would like force EchoStar and the cable systems to improve their product as well, to the benefit of pay-TV consumers. More specifically, the parties plan to explore aggressively expanding DIRECTV’s local-into-local service into more of the 210 local television markets. This is an important potential benefit, and we will examine carefully how the parties plan to expand that service, and we will examine other potential benefits as well.

Additionally, we must examine the concerns that have been raised about this deal.

First and foremost, we must examine concerns that this deal will lead to higher prices for both cable and DBS subscribers. In short, the scenario that critics fear most is one in which News Corp raises prices to DIRECTV, then wields DIRECTV as a club to batter cable companies into accepting higher prices as well, all at the expense of consumers.

More generally, critics of this deal have raised concerns about whether News Corp will use its additional leverage as an anti-competitive weapon to unfairly disadvantage other programmers and distributors. These are complicated issues that need to be examined very carefully.

To their credit, the parties have proposed ways to address some of these concerns. Specifically, News Corp has promised that it will abide by the program access rules, even under circumstances when those rules technically would not apply to a News Corp or DIRECTV combination. News Corp also plans to establish an Audit Committee of the DIRECTV board of directors, which would ensure News Corp deals fairly with DIRECTV.

We plan on exploring whether these protections are sufficient to ease the concerns that have been raised about this deal.

Finally, we also look beyond the confines of this specific deal to its broader implications for competition in the industry. This Subcommittee has to ask whether the News Corp or DIRECTV transaction will set in motion a series of mergers between larger content companies and distributors.

Such consolidation might leave the media in the hands of fewer and fewer vertically integrated companies, companies with enough

market power to effectively exclude independent programmers and raise prices, both to the detriment of American consumers and the marketplace of ideas.

Clearly, this is an important transaction which, if approved, would have a significant impact on how American consumers receive their news, their information, their sports and their entertainment. We have a lot to discuss today, and I look forward to hearing from our witnesses.

Now, let me turn to Senator Kohl, the Ranking Member of this committee.

Senator Kohl?

**STATEMENT OF HON. HERBERT KOHL, A U.S. SENATOR FROM THE STATE OF WISCONSIN**

Senator KOHL. Thank you, Mr. Chairman.

As you said, a little more than a year ago, we sat in this room to examine EchoStar's attempt to acquire DIRECTV. That deal would have created a monopoly in satellite television and limited most consumers to only two choices for pay TV—the cable company and one satellite company. We opposed that merger and, wisely, both the Justice Department and the FCC decided to block it.

This year, it is News Corporation's turn to try to acquire DIRECTV, a deal presenting an entirely different set of issues. One of the world's largest media conglomerates, with holdings ranging from the Fox TV network, the Fox News Channel, Fox Sports Net, FX cable networks, the Twentieth Century Fox movie studio, 35 broadcast television stations, to newspapers like the New York Post and magazines like TV Guide, is seeking to acquire the DIRECTV satellite system, the Nation's second-largest television distribution system.

This combination of content holdings with worldwide distribution will create a media powerhouse of virtually unmatched size and scope. The overriding fear is that News Corp/DIRECTV will take advantage of their global distribution system and must-have programming to raise prices and squeeze out competition.

Mr. Murdoch and Mr. Hartenstein will claim several benefits offered by this deal—a stronger DIRECTV, fortified by its corporate connection to News Corp, deploying new technologies better able to compete with cable TV. But, for us, the crux of the matter is what matters most to consumers—the deal's likely effect on the ever-rising prices paid by consumers for pay TV and on the choice and variety of programming available.

So, to convince us that this deal is truly in the public interest, Mr. Murdoch and Mr. Hartenstein must answer some difficult questions. Namely, will this deal create a vertically integrated media giant capable of raising the price of its programming and excluding other programmers from its powerful distribution network? And will this deal set in motion a chain of mergers as content companies and distributors find it necessary to merge to compete with News Corp/DIRECTV? And will this deal harm competition in the marketplace of ideas and further degrade the diversity of news, information and entertainment available to the American public.

News Corp has preemptively pledged to adhere to a number of commitments should this deal be approved. This demonstrates, we

believe, their understanding that antitrust authorities are going to have concerns. So we will ask you, Mr. Murdoch, to agree to several other legally binding and enforceable conditions, consistent with your already announced pledges. Your answers, we believe, will demonstrate whether you are truly serious about avoiding any injury to competition.

Mr. Murdoch, we will ask you:

Number one, to make all News Corporation programming, cable channels and broadcast TV stations available to DIRECTV's competitors on the same terms as they are made available to DIRECTV;

Two, to avoid any unreasonable price increases in the cost of NewsCorp programming;

Three, to allow News Corp programming rivals equal access to DIRECTV, including with respect to channel placement and tiering; and,

Number four, to work to substantially increase the number of markets covered by local-into-local service and broadband access with specific targets on specific dates.

To date, consumers of pay TV have continued to suffer ever-increasing prices and ever-greater consolidation. We need to examine this merger carefully to ensure that, for a change, the promised benefits are truly realized.

And so we thank our distinguished panel for being here today, and we look forward to having a full and complete discussion.

Thank you, Mr. Chairman.

Chairman DEWINE. Senator Leahy?

**STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR  
FROM THE STATE OF VERMONT**

Senator LEAHY. Thank you, Mr. Chairman, and I am appreciative of the fact that you and Senator Kohl are holding this hearing.

The merger, actually, the larger issue of media consolidation is very important to Senators on both sides of the aisle, and I commend the two of you for following what has been the normal bipartisan way you have approached these subjects. We are aware of the dangers of corporate consolidation, especially in the information and entertainment industries, where the First Amendment, as well as the antitrust laws, have significant roles to play. A hearing like this is very timely because we try to protect both the marketplace, but also our freedom of speech, which I feel the First Amendment, the most underpinning of our whole democracy.

Now, no one in this room could have missed the firestorm of debate and outcry that accompanied the Federal Communications Commission's recent changes in the media ownership rules. I know those changes do not directly touch on the merger here today, but they are a tangible piece of the puzzle we are all trying so hard to solve.

The Commerce Committee, I believe, is meeting tomorrow. We are going to have a hearing on media concentration next week, and meanwhile the FCC continues to roll back the regulations that were designed to preserve a diversity of programming options, a host of editorial choices and voices. And as soon as you could this



homogenization of programming, that is not going to help viewers or listeners.

I know it is true in a rural State like Vermont, where we have demonstrated with our town meetings that we like independence, and we like a diversity of views, but I suspect that is the same everywhere. Then, when you add the likelihood that increasingly powerful media conglomerates can raise the prices consumers pay, at the same time they can reduce the quality of their programming, both in quality, and in quantity, and in content and even technologically, the implications of unfettered media conglomeration to the American people and to our communities and to our society is very troubling.

I think that is where we are today. I wrote to the FCC, when the rule changes were under consideration, there are those who argue that the increase in the number of media outlets has obviated the need for the rules limiting media ownership. That is not so. The number of media outlets has increased and ownership has become more concentrated.

There are certainly fewer opinions among the American people than 1975, when these standards were established, but there are indisputably fewer true avenues for their expression to reach sizable segments of the population. To me, it is illogical that the FCC would exacerbate a disturbing trend which is transforming the marketplaces of ideas into little more than a corporate superstore.

The proposed deal between DIRECTV and News Corp is not implicated by these rule changes, but it is an unavoidable truth the atmosphere of concern created by the FCC's actions will color the evaluation of all media deals. Each time that the FCC eases some restriction, we are assured that the "public interest" inquiry that the Agency undertakes in such deals will ensure that consumers' legitimate interests are protected. Well, this merger is one deal where we should test that repeated assertion.

When the Nation's largest home satellite TV service is purchased by one of the world's largest media companies, it should come as no surprise that people are concerned about the choices consumers will have—something I have raised with Mr. Murdoch and others. Will the new entity discriminate against other distributors like cable companies, and especially small cable companies that serve a lot of rural areas.

What about content providers or are they going to pay for News Corp's own popular programming, such as shows on the Fox TV network, or the News Channel and sports channels?

Then, I have a couple others, and I will do them briefly, Mr. Chairman, other concerns, especially important to Vermont: The provision of local-into-local television to smaller Designated Market Areas, DMAs, and the roll-out of broadband service to underserved communities. Local-into-local is extremely important to my State. We have the largest percentage or per-capita percentage, I believe, sadly, dish owners of any State in the country. If it is not the first, it is certainly the second. That is because most of our areas cannot get cable. We need local-into-local to find local news and weather, if there is a flood, there is a dangerous condition or anything else.

Now, since July 2002, EchoStar has provided local-into-local television to its customers in Vermont. News Corporation has assured

me that they want to provide local-into-local TV to Vermont, but they have been unable to answer the question when they will do this.

The same holds true for broadband to these underserved areas. Again, News Corporation is hopeful they will be able to provide broadband to potential customers, but unable to provide any time frame. So these are among my concerns, Mr. Chairman. Again, I commend you for holding this hearing.

Chairman DEWINE. Senator Leahy, thank you very much. We will move to our panel. Mr. Rupert Murdoch, of course, is the Chairman and CEO of the News Corporation. News Corp's holdings include newspapers and magazine publishing on 3 continents, major motion picture and television production and distribution operation, as well as television, satellite and cable broadcast operations worldwide, and of course the Fox broadcasting channel.

Mr. Eddy Hartenstein is the Chairman and CEO of DIRECTV. He has headed DIRECTV since its inception in 1990 and is currently Chairman of the Satellite Broadcast and Communications Association. He has testified before this Subcommittee previously, and we welcome him back.

Mr. Robert Miron is the Chairman and CEO of Advance/Newhouse Communications, which manages cable television systems serving over 2 million customers. He was elected to the board of directors of the National Cable Television Association in 1983, serving as an officer and member of the Executive Committee for a number of years. He is testifying here today on behalf of Cable One, Cox Communications and Insight Communications.

Gene Kimmelman is the senior director of Consumers Union. He is widely respected as an advocate on a broad range of issues in both the areas of cable television and antitrust law. Prior to his tenure at Consumers Union, he served as chief counsel for this Subcommittee and has been a frequent witness for us in recent years. Gene, thank you very much for joining us once again.

Scott Cleland is the CEO of the Precursor Group, an independent research/broker dealer. He has testified before numerous Congressional panels on a variety of antitrust and telecommunications issues, including this Subcommittee, and we welcome him back as well.

We will follow a 5-minute rule. We are going to be strict about that today because we want to have a lot of time for questions. So we are going to start with Mr. Murdoch. We have your written testimony from everyone, and it is part of the record. We appreciate that. And if you could just give us your summary, anything else that you would like for us to hear.

Mr. Murdoch, thank you.

**STATEMENT OF RUPERT MURDOCH, CHAIRMAN AND CHIEF EXECUTIVE, THE NEWS CORPORATION, LTD.**

Mr. MURDOCH. Thank you very much. Good afternoon, Chairman DeWine.

Chairman DEWINE. And all of these mikes have to be activated. They are no longer the old mikes where you just spoke into them that we used to have in this Committee. Now, you have to push the button.

So, Mr. Murdoch, you are first.

Mr. MURDOCH. Good afternoon, Chairman DeWine, Senator Kohl, Senator Leahy. Thank you for this invitation to testify today on News Corporation's proposed acquisition of a 34-percent interest in Hughes Electronics Corporation. This transaction will infuse DIRECTV with the strategic vision, expertise and resources necessary to bring increased innovation and robust competition to a multichannel market. The resulting public interest benefits are manifold and substantial. Today, I would like to tell you specifically why this deal will be good for consumers and good for competition.

By combining the expertise and technologies of our two companies, consumers will benefit from the better programming, more advanced technologies and services and greater diversity that we will provide. One of the first enhancements DIRECTV subscribers will enjoy is more local television stations, with the first component of local-into-local service as part of our BSkyB satellite venture 6 years ago, and it remains one of our top priorities.

News is committed to dramatically increase DIRECTV's present local-into-local commitment of 100 DMAs by providing local-into-local service in as many of the 210 DMAs as possible and to do so as soon as economically and technology feasible.

In addition, News is exploring new technologies that promise to expand the amount of high-definition television content on DIRECTV, and News will work aggressively to build on the broadband services already provided by Hughes.

News will also bring a wealth of new services direct to DIRECTV subscribers from BSkyB in the United Kingdom, including interactive news and sports and access to on-line shopping, banking, games, e-mail and information services, and we will infuse Hughes with our deep and proven commitment to equal opportunity and diversity, including more diverse programming and a variety of mentoring, executive development and internship programs.

You can count on these enhancements because innovation and consumer focus is in our company's DNA. We have a long and successful history of defying conventional wisdom and challenging market leaders, whether they be the "big three" broadcast networks, the previously dominant cable news channel or the entrenched sports establishment.

We started as a small newspaper company and grew by providing competition and innovation in stale, near monopolistic markets. It is our firm intention to continue that tradition with DIRECTV. With these consumer benefits, DIRECTV will become a more formidable competitor to cable and thus enhance the competitive landscape of the entire multichannel industry.

To that end, I should note that there are no horizontal or vertical merger concerns arising from this transaction. The transaction does result in a vertical integration of assets because of the association of DIRECTV's distribution platform and News Corp's programming interests, but this is not anticompetitive for two reasons:

First, neither company has sufficient power in its relevant market to be able to act in an anticompetitive manner.

Second, neither News, nor DIRECTV, has any incentive to engage in anticompetitive behavior. As a programmer, News Corp's

business model is predicated on achieving the widest possible distribution to maximizing advertising revenue and subscriber fees. Similarly, DIRECTV has every incentive to draw from the widest spectrum of attractive programming, regardless of its source.

Nevertheless, we have agreed to a series of program access undertakings to eliminate any concerns over the competitive effects of this transaction. We have asked the FCC to adopt these program access commitments as a condition of the approval of our application.

Viewed from another perspective, neither News, nor Hughes, is among the top five media companies, by expenditure, in the United States. As you can see in the chart attached to my testimony, News is sixth, with 2.8 percent of total industry expenditures, and Hughes is eighth, with 2.2 percent. Even combined, the companies would rank no higher than fifth, half the size of the market leader.

In closing, I believe this transaction represents an exciting association between two companies, with the assets, the experience, and the history of innovation to ensure DIRECTV can provide better service to consumers and become an even more effective competitor.

Thank you for your attention. I look forward to your questions.

[The prepared statement of Mr. Murdoch appears as a submission for the record.]

Chairman DEWINE. Mr. Hartenstein?

**STATEMENT OF EDDY W. HARTENSTEIN, CHAIRMAN AND  
CHIEF EXECUTIVE OFFICER OF DIRECTV, INC.**

Mr. HARTENSTEIN. Chairman DeWine, Senator Kohl, Senator Leahy and members of the Subcommittee, who I presume will come, I appreciate the opportunity to tell you why the split-off of Hughes from General Motors and the purchase of a 34-percent interest in Hughes by News Corp. will benefit consumers throughout the United States, whether they are current or prospective DIRECTV subscribers, or even current cable subscribers.

As a direct result of this transaction, DIRECTV will be able to improve its service offerings and provide a stronger, more competitive alternative to cable. Until 1994, there were no serious competitive alternatives to the dominant cable operators. With the launch of DIRECTV, exactly 9 years ago yesterday, consumers gained access to an alternate provider that offered more channels, and superior picture and sound quality. But it was not until November of 1999, when Congress changed the law to allow satellite carriers to retransmit local broadcast channels, that DBS was able to truly offer a competitive alternative to cable, at least in those markets in which DBS operators, such as ourselves, provide local channels.

The benefits to consumers from DBS competition to cable have been tremendous. In a direct response to DBS competition, cable operators have aggressively upgraded their services, and it is forecast that in the very near future, for the first time, the number of digital cable subscribers will exceed the total number of DBS subscribers in this country.

Such developments underscore the need for DBS operators to keep pushing the competitive envelope to preclude satellite TV customers from being left behind. DIRECTV is already on this course.

Today, we offer local channels in 61 markets and are on track to meet our goal of more than 100 markets, upon the successful launch of our eighth satellite by year end. In just 12 days, we will expand our high-definition television programming services to 6 channels nationwide.

But we simply cannot stop there. In order to continue improving our services, it is critical that we keep expanding DIRECTV's programming offers and keep providing new and innovative services to consumers.

At a time when DIRECTV requires capital to continue to innovate and compete, however, GM is focused on improving its core automotive operations and addressing the need to provide funding for its U.S. pension plans. DIRECTV must pursue new initiatives to remain competitive with cable, which will require additional funding.

GM cannot provide such funding because of the resulting downward pressure on GM's credit rating. GM has recognized that an independent Hughes and DIRECTV will have more flexibility to obtain the kind of financing that it—DIRECTV—needs to continue to grow and stay competitive into the future.

GM identified with us News Corp. as an ideal partner for Hughes and DIRECTV because of its proven track record as a global direct-to-home service provider. And with News Corp's support, we intend to increase the number of television markets in which DIRECTV provides local broadcast channels as quickly as technologically and economically feasible. Consumers residing in those local markets will be able to obtain satellite-delivered local news, weather and sports, and cable operators in those same smaller markets will be forced to improve their services in response. For those consumers, it is a win-win.

Through our combined efforts, we intend to expand even further the number of high-definition channels that we offer which, in turn, should accelerate consumers' adoption of high-definition reception equipment nationwide.

Historically, News Corp. has produced and supported a wealth of culturally, ethnically, and linguistically diverse programming through its Fox film divisions, television network and broadcast stations. We plan to tap into News Corp's resources to expand DIRECTV's already diverse program offerings.

In sum, the future looks bright for DIRECTV. Independence from GM and the investment by News Corp. will allow DIRECTV to improve and expand its services for consumers, a result that will be manifestly in the public interest.

Now, I realize, Chairman, Senator, that I appeared before this very Subcommittee just over a year ago touting the benefits of a different transaction. As you know, the Justice Department and the FCC prevented us, as you suggested, from consummating that transaction. I believe that the current transaction raises none of the concerns that the DOJ and the FCC cited in connection with the prior transaction, and for that reason, I am hopeful that those agencies will allow us to move forward quickly with the News Corp. transaction so that we may continue aggressively to pursue the strategy we have pursued since our launch in 1994, which is to offer the best competitive alternative to cable possible.

I appreciate the opportunity to share my views and look forward to your questions.

Thank you.

[The prepared statement of Mr. Hartenstein appears as a submission for the record.]

Chairman DEWINE. Good.

Mr. Miron?

**STATEMENT OF ROBERT MIRON, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, ADVANCE/NEWHOUSE COMMUNICATIONS**

Mr. MIRON. Thank you, Mr. Chairman.

In addition to our company, I am testifying today on behalf of Cable One, Cox Communications and Insight Communications. Together, these companies serve nearly 10 million cable television homes in 31 States. We thank you, Mr. Chairman, and we thank Senator Kohl and Senator Leahy for this opportunity.

No doubt, News Corp's acquisition of DIRECTV can benefit competition. However, what we find troubling is that the acquisition will give News Corp unique and unprecedented power and incentive to raise the cost of programming to providers, and thus consumers in all three multichannel platforms: cable, Direct and EchoStar.

Our concerns are magnified by the possibility, and perhaps even the likelihood, that this transaction will be followed by a similar consolidation involving EchoStar. Today, there are vertically integrated companies that combine powerful programming assets with cable system ownership, but no cable company currently has the potential to serve more than about one-third of American homes. None comes to close to the geographic reach of Direct, which is present in every television market. None currently owns broadcast stations inside cable markets, while News Corp owns and operates 35 stations within Direct's national service area, including 9 in the top ten markets and 16 in the top 20.

It is already hard enough to negotiate with the 4 companies that combine ownership of broadcast networks, broadcast stations and cable networks. Retransmission consent negotiations involve not just the carriage of broadcast stations, but how much cable operators will pay to the broadcast stations' affiliated cable networks and how many new affiliated networks they will need to carry.

Inevitably, cable operators face demands for carriage of these affiliated channels on their most watched tier of programming, so that all of our customers have no choice but to pay for them.

Like network-affiliated broadcast stations, regional sports networks are must-have programming. They present much the same set of negotiating problems for cable operators, and News Corp controls, by far, the largest collection of regional sports networks. News Corp's 18 regional sports networks cover 10 of the top 20 television markets, and each is combined with an ownership of a Fox-affiliated broadcast station.

Today's marketplace is workable only because both EchoStar and Direct approached their negotiations with programmers from much the same point of view as cable does. Once Direct becomes a partner of the News Corp stations and networks, our negotiating position will be severely compromised. If a cable operator fails to reach

carriage agreements, it will be granting its competitor de facto exclusive carriage of very desirable programming. That is not acceptable, and operators will be forced to concede. So will EchoStar. Prices will go up for Direct customers, EchoStar customers and cable customers.

We believe the impact will be substantial nationally. It will be even more severe for small- and mid-size cable operators, many of whom operate in smaller markets and rural areas and who typically pay higher prices for programming than does Direct.

News Corp has recognized there are problems and has proposed two conditions:

First, they have proposed to comply with the FCC's program access rules, but News Corp has exempted its broadcast stations from the program access commitment. The Fox stations are the big dogs of News Corp's programming complex. Failure to include them in the program access commitment greatly reduces its value.

Of equal importance, the program access rules allow News Corp to use the additional power it will gain from control of Direct to raise rates for cable television and EchoStar, so long as they avoid discriminating by also raising rates to Direct. We believe they have the incentive to do just that.

Second, News Corp has proposed subjecting related-party transactions to review by an independent Audit Committee of Direct's board. But Audit Committees are best-equipped to find harm to shareholders' interests. Here, the harm is to the marketplace and consumers, not to Direct or its shareholders. Finding this harm is beyond the mandate and the ability of the Audit Committees and independent directors.

In our view, News Corp acquisition can operate without harm to the public interest, but only if appropriate conditions can be constructed, in addition to those already proposed, to limit the adverse effects on consumer prices for DBS and cable television.

Thank you.

[The prepared statement of Mr. Miron appears as a submission for the record.]

Chairman DEWINE. Mr. Kimmelman?

**STATEMENT OF GENE KIMMELMAN, SENIOR DIRECTOR FOR  
ADVOCACY AND PUBLIC POLICY, CONSUMERS UNION**

Mr. KIMMELMAN. Thank you, Mr. Chairman. On behalf of Consumers Union, the Print and on-line publisher of Consumer Reports magazine, I appreciate the opportunity to testify this afternoon about consumer concerns with the News Corp/DIRECTV merger.

Senators DeWine, Kohl and Leahy, you will recall, in 1996, Congress passed the Telecommunications Act which launched deregulation of cable television on the theory that satellite television was there to compete against cable, to hold prices down.

Well, today, prices are more than 50-percent higher than they were then, rising almost 3 times faster than inflation. Unfortunately this deal will not stop that. As a matter of fact, it may make matters worse. Prices will continue to rise. I hardly ever agree with the cable industry, but I believe Mr. Miron has it exactly right—prices will just keep going up.

In the context of the FCC's recent decision to relax media ownership rules, just think of what companies, like News Corp with DIRECTV, will also be able to do: buy a second or a third local broadcast television station in communities across the country, buy the dominant—no, not the dominant—the monopoly newspaper, add more cable properties, radio stations, become the dominant source of local news and information in communities across the country.

Tomorrow, the Senate Commerce Committee will begin taking action to undo the FCC's relaxation of media ownership rules, bringing back a promotion of diversity and competition in local news markets. I hope you will join in that effort. But until the FCC's decision is overturned, this transaction, and others likely to spring out of this, pose enormous dangers to consumers.

How is that the case? Well, think of it on the national level. News Corp owns a national television network with rights of carriage on all cable systems across the country, 30 broadcast television stations, a major stake in more than 20 cable properties with rights to the most popular professional sports leagues and teams, 67 professional sports teams that are the basketball, baseball and hockey favorites in communities across the country, in-house production studios, and newspapers here and abroad.

Then, this company can add more properties at the local level, a second, a third local broadcast station, and newspapers, and on and on. Is this good for competition? Does this bring more diversity of views from different owners? On the contrary. It consolidates, at a dangerous level, the power of few entrepreneurs, with First Amendment rights to control their media properties, to define what news and information is in the local market, to present it as they see fit, and to, unfortunately, undermine the potential for competition across all technologies, the kind of competition we hope for with deregulation.

I believe consumers' interests cannot be served by this transaction unless significant conditions are imposed by the FCC, by the Congress, and very strict antitrust enforcement is pursued to ensure that prices do not rise for cable and satellite customers. Why would they rise? Just think about it. With all of those stations, all of those cable properties, and the very expensive television rights to professional sports teams, Mr. Murdoch is in the position of bundling that programming and raising the input costs for all of his satellite and cable competitors. His promise will do nothing to prevent prices from going up. As a matter of fact, it enables him to signal the market that everyone's prices go up. Cable may not like it, but why not pay those higher prices, when every satellite company also pays those prices. Everyone pays more, the consumer pays more. That is not the kind of competition that benefits the marketplace.

So we believe antitrust officials, through tough enforcement, that conditions placed on this deal by the FCC are absolutely critical, and most importantly, we believe Congress must act. It is time to overturn the FCC's relaxation of media ownership. It is time to prevent consolidation of multiple broadcast, cable and newspaper properties with content distribution. And it's time to prohibit companies like News Corp, combined with DIRECTV, and others with



market power over distribution systems from preventing consumers, choice to pick the programming they want, get it at a fair price while ensuring that there is competition in the marketplace.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Kimmelman appears as a submission for the record.]

Chairman DEWINE. Mr. Cleland?

**STATEMENT OF SCOTT CLELAND, CHIEF EXECUTIVE OFFICER  
OF THE PRECURSOR GROUP**

Mr. CLELAND. Mr. Chairman and Senators Kohl and Leahy, thank you for the honor to testify as an independent analyst who represents institutional investors in our business.

My overall view, when you look at this merger, from an antitrust perspective, is I do not think this merger is anticompetitively going to hurt consumers and competitors. So while I think it does not necessarily raise antitrust concerns, I do think there are legitimate and significant First Amendment and public policy issues that are raised by this that are most appropriately dealt with in the FCC arena or in the legislative arena, but not necessarily as conditions to a merger.

Now, we also, my Precursor Group, when we talk to investors about this, you should also know we have advised them we thought that this deal would get approved by the Government and that we thought it would create value.

Now, what I think I can do for you today that is helpful and give you some insight is I think this deal is a lot less about pricing than it is about technology and about correcting some business-model weaknesses, and so I would like to run through 7 dynamics that are going on with News Corp that are motivating News Corp and DIRECTV to get together. This is not just about negotiations or pricing.

The first is, is they need to make the transition from analogue to digital. As you all know, the over-the-air broadcast has been, the transition to digital has been snake-bit, and very slow, and very expensive. It is essentially all pain and no gain.

With this transaction, they can make the leap from an analogue business model to a digital model.

In one leap, they also can go from a regional platform to a national platform, the second thing.

The third thing is they are going to be able to change their business model from an advertising-based model, which is very economically sensitive with economic cycles to a subscription-based model which is less-economically sensitive. It will also allow them to go from single channel to multichannel. The clear trend in pay TV is towards niche programming and having the technology that enables you to narrow cast and have many channels is the wave of the future. So this enables them to do that.

The other thing it does is it allows them to move from a very unsecured platform to a more secure platform. You have over-there broadcasters up here asking for help because the technology today enables people to easily pirate digital content. And when you make a digital copy of one copy, you can make a billion of them. And so the technology here, and there is a need and a desire for News

Corp to move its content off of an analogue, more vulnerable, easily pirated technology, to one where they have more control to protect their value.

The other thing is that they are making a shift from a depreciating business model to an appreciating one. I mean, they are shifting horses kind of mid race. The over-there broadcast model is way past its prime. It should be put out to pasture, and essentially the DBS technology is more like a thoroughbred, and they are switching horses I think quite wisely.

And the last thing is, and that is the subject of this discussion and why you all are having this very important discussion, is that it does shift from an unleveraged business model to a leveraged one, and the reality is, is when you are negotiating, and Mr. Miron is right, is that you do have more negotiating leverage, you are taken more seriously at the negotiating table when you are a content provider and when you are a distributor. So that does create legitimate issues that should be discussed here.

Now, what I also would like to give you some insight is about what may be coming down the pike. I think Mr. Murdoch, at least from an investment standpoint and a business standpoint, is making the right decision. He recognizes these very serious business-model weaknesses, and for 6 years has tried to merge with a DBS provider.

I am surprised that Disney and Viacom do not share the strategic vision, and I believe, in the future, you will probably see a transaction that will involve EchoStar coming at you down the pike.

So, to wrap up, I do not think that this is an anticompetitive deal. This does not raise any more issues than, say, the Comcast/AT&T issue did, and I would also like to point out that one of the interesting things, as a kind of independent observer, is that News Corp has consistently been what is called a "maverick" competitor. They are an insurgent. They tend to be very disruptive and very good for the marketplace.

My time is up. I will conclude.

Thank you very much, Mr. Chairman.

[The prepared statement of Mr. Cleland appears as a submission for the record.]

Chairman DEWINE. Well, we thank you very much. You all gave very interesting testimony, and you all were right on time, too. I appreciate that.

We have a vote that started. We are going to stop now, and we will be back in 12/13 minutes, probably.

[Recess from 3:22 p.m. to 3:41 p.m.]

Chairman DEWINE. Mr. Miron, Mr. Kimmelman, you paint kind of a scary picture for us, and I would like to explore that with you and then try to get Mr. Murdoch's response.

Mr. Miron, let me put it on a personal basis. I am a Cincinnati Reds fan, I also have DIRECTV, and so I get the Cincinnati Reds on Fox Sports Net. I watched them last weekend when I was home in my home in Cedarville, Ohio. My dad is a Cincinnati Reds fan. He watches them in Yellow Springs, Ohio, on cable TV. He also, of course, watches them on Fox Sports Net.

So you are telling me that we both should be nervous about this deal? We are going to be paying more, are we, Mr. Kimmelman, Mr. Miron?

Mr. KIMMELMAN. I would like to answer—

Chairman DEWINE. It is bad for us as consumers, is it?

Mr. KIMMELMAN. I think it is, Mr. Chairman. Being a born Cincinnati, a Cincinnati Reds fan ever since I think I was 5 years old—

Chairman DEWINE. You are ingratiating yourself to the Chairman, I can tell, Mr. Kimmelman, but that is okay. That is all right.

[Laughter.]

Mr. KIMMELMAN. It happens to be true. If I still lived in that territory, I would be extremely worried because I know that one of the main reasons I would want cable or I would want satellite would be to watch the Reds.

Chairman DEWINE. Frankly, it is the only reason I got DIRECTV, and that is the truth. It certainly was not to watch—well, we will not go into that.

[Laughter.]

Mr. KIMMELMAN. I would be concerned that if Mr. Miron was my cable operator, and I was sitting there and was being told that because the price went up he was considering not putting it on the air, I would have to look at DIRECTV because I want it.

Now, like many consumers, there is a lot of frustration about the cost of cable going up and the inability to choose the channels that you want. Most consumers only watch about a dozen channels, and yet they get 50 or 60, and they have to keep being told that you should be happy to pay more because you are getting more, and they do not want them.

What I am afraid, we wanted satellite to be the kind of competitor that would come in aggressively and would challenge cable with discounts, and they have tried, to some extent. Their equipment costs are very high. Mr. Hartenstein is absolutely right. They have done an admirable job, but their costs are high, and getting a second set hook-up and getting a high-speed service is expensive, and it just has not so far really cut into cable price increases, unfortunately.

And what I am afraid of is this transaction, with a company that makes a lot of its money from programming, and the ability to bundle that with its over-the-air network and say, This is what we are charging. If you do not want it, you are not going to have it on your cable system. We will just put it on DIRECTV, is likely to raise prices for everybody.

Chairman DEWINE. Mr. Miron, do you want to weigh in here?

Mr. MIRON. Thank you, Mr. Chairman. I, too, was a—I remember Johnny Bench, and Joe Morgan, and was a fan.

I think our goal is really to protect the uninterrupted flow of Fox product to consumers at reasonable prices. And this transaction could undo that, since all 3 platforms now, today, negotiate and everybody tries to get the best price, and things could change if Mr. Murdoch owned DIRECTV. DIRECTV could make a deal to carry Fox Sports at a higher rate and then negotiate with the cable company to pay the same rate. If the cable company refused to pay

that rate, Direct would, in effect, have de facto exclusivity of that product.

And if the cable company could not stand the pressure, Cincinnati fans would want to go subscribe to DIRECTV, they would give in and pay the price, and that would have a tendency to force the prices up. I think that is one of our serious concerns.

Chairman DEWINE. Mr. Murdoch? Should I be afraid, Mr. Murdoch? Should my father be afraid of this? What is your answer to that?

Mr. MURDOCH. I do not think so, Mr. Chairman. I cannot claim to be a fan of the Cincinnati Reds, and I am sorry.

Chairman DEWINE. No, I hope not. I would surely hope not. I was waiting for that one.

[Laughter.]

Mr. MURDOCH. But the fact of the matter is the marketplace handles this. We do not—we were quoted as owning 18 or 19 regional sports networks—we, in fact, control only 10 of those. Our name is carried on about 19, and then we now have a small minority or they are associates of ours.

If I could quote a, it was a private conversation with Mr. Ergen of EchoStar a couple of months ago, saying, Thank God for Fox because it brings all of these teams together and charges like \$1 or \$1.50 a month, depending on what tier they are on or whatever, if each team, otherwise each team will have its own network like the Yankees, and everybody paying about \$8 a month.

And I think Fox provides a very good service here. It also provides a limited sort of competition to ESPN, which is much needed, and I am sure Mr. Miron would agree with that.

I do not know what they are going on about. I mean, our record here on pricing—first of all, let me just say this. Direct's record, it launched in 1994 with 50 channels at a price of \$29.95. Today, it sells its biggest package of 100 channels for \$33.99, an increase, over 9 years, of \$4.04, totally unlike our friends down the table here.

Fox has been dealing productively with the cable industry for years, giving them programming they want, on mutually acceptable terms, and at the same time getting the value from retransmission consent that Congress envisioned in the 1992 Cable Act in growing our business.

Retransmission consent is something quite different to program access. One applies to cable and satellite or we are making it apply to satellite, and the other has to do with broadcasting. And all we ask for is a level playing field. If they want to change that statute on retransmission, let them go ahead. It has got to apply to everybody. The effort of Mr. Miron and his associates here is simply to try and stop us from being competitive in any way they can.

On this question of our relationship with cable, the smallest cable systems that have Fox programming on them, 300 of them, they just were granted retransmission consent without any conversation, without even any discussion. The major ones, perhaps the biggest 10 companies, have more like 90 percent of the market. I think 6 companies have over 80 percent of the market.

We do, indeed, negotiate with and see what we can get. And we have had over the last couple of years I think 150—I have got them

here—separate deals for carriage on those cable companies for cable channels, which we have started. Our record, wherever you look, has been as a price-cutter, as a competitor and as a provider of new choice in what we do, and we intend to continue that here.

What really shocks me, frankly, is that Mr. Miron has allowed himself to be used by Cox to front for this effort here. They are privately owned entity, they are the fourth biggest cable operator in the country, they have programming services, they have leading, big TV stations—a bit more about that in a minute—large monopoly newspapers and many multi-radio station groupings in different cities.

In fact, when Mr. Kimmelman was sort of fantasizing about the future of News Corp, I thought he was describing Cox Communications today.

To get Fox News started, for instance, we have had to pay special payments to cable companies of over \$640 million. Fifty-one million of that went to Cox, in addition to which they made us sign a 10-year unbreakable, exclusive affiliation agreement for their large television station in San Francisco, which stops News Corp or Fox from really ever having an investment in television in San Francisco, a major market.

So they are well able to, they are big boys, they are quite capable of looking after themselves. I am not complaining. These have been vigorous negotiations, but to cry poor and to try and tie us down is something which I think is just outrageous.

Chairman DEWINE. Mr. Miron, do you want to respond to that?

Mr. MIRON. I certainly cannot respond to the particulars of the Cox situation, but we certainly do not believe any of the issues we are raising will have a limiting effect on Direct's ability to compete. We are simply concerned, and we have had negotiations with Fox over the years, and they are strained, but we have always managed to eventually come to an agreement.

We have had an occasional service interruption, but we think that, with DIRECTV, the incentive for possible, for this to change, would be much greater, and so we have genuine concern that if this happens, it will create some, as I said before, de facto exclusive product programming.

Chairman DEWINE. Mr. Kimmelman, and then my time is up, and we will turn to Senator Kohl.

Mr. Kimmelman, last comment.

Mr. KIMMELMAN. Mr. Chairman, I would just like to respond on this level. We certainly have problems with Cox, where it dominates the market, and we have raised concerns in the media ownership proceeding about some of that, but we did not have time, in the 5 minutes, to go through all of what News Corp owned here that is relevant to the Cincinnati Reds situation.

Mr. Murdoch owns substantial stakes in the Dodgers—

Mr. MURDOCH. They are for sale.

Mr. KIMMELMAN. The Lakers—

[Laughter.]

Mr. KIMMELMAN. The New York Knicks, the New York Rangers, Dodger Stadium. I mean, he owns it all the way up the chain for many of the sports franchises which are must-see local programming in the community. I have now testified with him 3 times be-

fore Congress in the last month. I have not once heard him that he can make cable rates go down through his transaction, that he is going to compete down prices.

He has got a different vision of competition. It is admirable, it provides some benefits. I do not disagree with that, but let us be clear here. There is nothing about this transaction that appears likely to drive prices down for watching the Reds or any other team.

Mr. CLELAND. Could I add to that comment, just to give an insight into the cable market?

Chairman DEWINE. Sure.

Mr. CLELAND. I agree, you know, cable rates have not gone down, but generally the DBS pay TV is not a competitive market. It is a Government-manufactured market. There were 4 DBS licenses that were granted. The market would only fund two. EchoStar and DIRECTV are the only ones that survived. And so the reality is we have a 3-person market. Generally, in a 3-provider market, you have competition on service, on packaging, those types of things. Generally, they know, it is oligopoly, they look around, and they say, We do not want to compete on price. It is in none of our interests, and generally it takes a fourth or a fifth or a maverick pricer. And as I said before, I think News Corp is an unusual one in that they have a history of being a maverick pricer and a maverick competitor.

Chairman DEWINE. Senator Kohl?

Senator KOHL. Thank you, Mr. Chairman.

Mr. Murdoch, Mr. Hartenstein, for weeks we have heard you making the promises in order to convince us that your deal will, in fact, be beneficial to consumers. It has been our experience that these promises are soon forgotten, and consumers fail to see sufficiently of the benefits.

I would like to discuss your commitments in detail, but before doing so, I would like to ask one question. Are you both willing to commit here today to be subject to an enforceable and legally binding decree either at the FCC or Justice Department that you will implement your promises if this merger is approved?

Mr. MURDOCH. Yes, sir. That is a condition of the deal. We have written that in and offered that.

Senator KOHL. Good.

Mr. HARTENSTEIN. Absolutely, sir.

Senator KOHL. Good. Mr. Murdoch, your commitments do not limit your ability to raise prices for your programming, as long as you do so on the same terms that you do to DIRECTV; is that a fact?

Mr. MURDOCH. I am sorry, Senator. You mean that there has been a suggestion that we might raise the price of our programming that we sell to Direct and then try to let it run through. The fact is we do not have that power. It would not be a thing we do because of Direct, it would be because the programs are good, and we would be doing it already. We charge what the market will bear, frankly.

Then, there is the other matter, if you think of anything sort of out-of-line that could be done, there is, in spite of all that has been said, a very strong majority of independent directors that are there

to look after all of the shareholders. I know we have that in a parallel situation in BSkyB in Britain. It has taken us nearly 3 years to get a Fox channel on for 7 miserable cents per month.

These Audit Committees do operate for all of the shareholders, so we are not going to put anything that is uneconomic on Direct. We could not get away with it.

Senator KOHL. I do appreciate that. I was simply referring to your ability to do it. Not that you might or might not do it, but that you can do it.

Mr. MURDOCH. I cannot.

Senator KOHL. You cannot do it?

Mr. MURDOCH. No, I cannot do it because it would go to the—every transaction has to be, between any affiliated company or our company, has to be approved by the Audit Committee of the company, who are independent directors and distinguished businessmen in their own rights, and they are not going to be party to Direct paying anything that is unfair.

I mean, you can say they are only worried about the shareholders, not about the public—

Senator KOHL. I do not have a sense of sufficient comfort, with respect to the Audit Committee and its independence.

Mr. MURDOCH. Well, sir, if I might just, you know, it does fully comply with all of the rules of the FCC, and with the New York Stock Exchange, NASDAQ and the new Sarbanes–Oxley Act. I cannot say more than that.

Senator KOHL. Do you want to comment on that, Mr. Kimmelman?

Mr. KIMMELMAN. Senator Kohl, I would just like to say that no one is suggesting News Corp is going to break the law, and no one is suggesting it is particularly unfair to raise your prices if you can get away with it. If cable has to pay a higher price for the Fox network, for FX, for Fox News, for the regional sports channel, and EchoStar has to pay that same higher price or a higher price, then it is not harming DIRECTV to pay approximately that price.

And given that they are allowing for volume discounts in their own commitments, they are, with 11 million subscribers, one of the largest-volume providers of multichannel video service, they can probably justify a somewhat lower price than most cable operators or EchoStar would pay.

So the terms “fairness” or “legality” are not the issue here. If the point is will prices go up or go down, I have not heard a word that indicates to me that there is any likelihood they will go down.

Senator KOHL. Mr. Murdoch, the Audit Committee will not stop any deal as long as the cable pays the same price. I mean, that is almost self-evident.

Mr. MURDOCH. If we went to the cable companies first and said, Hey, we want to double all of our charges, and if you do, we will make Direct pay it, you are probably quite correct, but I do not see that happening.

Cable, sir, has 80 percent of the market. It is almost a de facto monopoly. Direct has 12 percent of the market.

Senator KOHL. Another question, Mr. Murdoch.

In the past, you have imposed substantial program rate increases. For example, the Washington Post reported that this year

you raise the cost of your Fox Sports programming by more than 30 percent to some cable operators. Would you agree to limit raises and the prices charged for your programming? For example, would you commit not to raise prices for your programming to no more than the national average rate of cable price increases over the past 5 years?

Mr. MURDOCH. I would have to study that, what the figures are. I do not know of any 30-percent increase. The fact is that all of those charge different prices, and it is sort of a jumble, and there has been a leveling, although some people may have gone up, but it is nothing like ESPN which goes up 20 percent every single year.

Who knows. We are not trying to put those prices up. We are just trying to keep what we pay the teams down.

Senator KOHL. I think it is essential that the regulators craft some reasonable restrictions on your ability to raise programming prices as a condition of approving this deal. That is an opinion that I hold.

Mr. MURDOCH. Well, let me take an instance where I think we were entitled to an increase which we will not get for 2 or 3 years because we have a binding legal contract. But Fox News, for instance, gets about half what CNN gets, and yet we deliver double the audience, and you know when those contracts come up, we will certainly look to correct that. I think that is a reasonable economic objective. It is a reasonable business approach.

Senator KOHL. Gentlemen, while you have agreed to make your cable television programming available on a discriminatory basis to cable and satellite companies, you have not committed, Mr. Murdoch, you have not committed to do so with respect to your 35 broadcast television stations. And your Fox broadcast stations are among the most powerful programming forces, as you know, in television.

Fox is one of the top 4 national networks, one that has popular programming, like professional football, that to many viewers is essential. And yet without such a nondiscriminatory commitment, you could threaten to withhold the rights for EchoStar to any cable or any cable system to carry any Fox network affiliate in exchange for favorable terms, such as the carriage of other News Corp cable systems or programming.

Mr. Miron, are you concerned about this scenario, and why do you believe it is dangerous?

Mr. MIRON. Senator, I would love to comment on a couple of things that Mr. Murdoch said.

First, he made the statement that Fox News had a greater rating than CNN and his price was half. We could look at it the same way and say that Fox News has a rating that is greater than the sports channels that he delivers to us, but the sports channels have a far greater rate, and if he wanted to equal the rating, that would be interesting.

He said that he will charge what the market will bear. I think that really was the key statement, and I think what we believe is that this transaction will give him added market power, and that added market power, coupled with his statement that he will charge what the market will bear, will bring higher prices to the consumers.



Senator KOHL. Mr. Murdoch, will you agree that you will make your broadcast television stations available to competing satellite and cable TV systems on the same terms as they are made available to DIRECTV?

Say yes.

[Laughter.]

Mr. MURDOCH. Each transaction is different, but broadly speaking here, but I better look at that before I bind myself on that, sir. Let me just say this. It is absolutely essential, whether it is a cable channel or whether it is our local television station to get every conceivable pair of eyeballs watching you.

You do not just go and take yourself away from 80 percent of the market and say we are not going to have this cable system in this city because we do not like Comcast or something or cannot get an agreement with them. That would be totally self-destructive. It is just not possible. The same with, I mean, why do you think I paid, you know, hundreds and hundreds, and probably well over a billion dollars to get cable channels established and get distribution for them?

You know, we have bled a lot of money waiting for cable companies, big cable monopolies, to move in their own good time. And we even had Time Warner bar us from the essential market of New York because they own a rival news channel. We had to go to court, we had to fight, we had a huge political fight before we could finally settle that. We are not dealing with a bunch of virgins here.

Senator KOHL. So was your answer yes or no?

Mr. MURDOCH. I am not prepared to make commitments about our broadcast license that I would not want to see a majority governed by statute, and I would want to see, if there is a change in that, would that—of course, we would have to agree to any statute—but how would it apply to our competitors? It is a different world, and if we had to do something which NBC, and CBS and ABC are not committed to do, I would have to just approach that with some caution.

But if you said would we not charge more than what we would charge Direct or we would do the same, I think that is a reasonable request, but I just, before committing myself, I would really need to talk to my advisers and study it.

Senator KOHL. Sure.

Mr. Kimmelman?

Mr. KIMMELMAN. Senator Kohl, in 1992, Congress, at the request of the broadcast industry, granted automatic carriage to broadcast networks and the right to bargain for retransmission consent based on one very simple set of facts. Cable was the dominant means by which the American consumer was receiving broadcast network television, and broadcast networks had to go through the cable system. They did not own another transmission system.

I will tell you what the difference between News Corp with this transaction is from NBC, CBS and ABC. It owns a new transmission distribution system through DIRECTV. Those companies do not. It has a national network and a satellite distribution system nationwide. The logic of the granted rights by Congress does not, and should not, apply to News Corp if this transaction goes through. The facts will no longer fit the circumstances.

Senator KOHL. Mr. Miron, how important is access to sports for cable programmers? What would happen if your customers could not see the local sports teams in their areas because another distributor had exclusive rights to these broadcasts?

Mr. MIRON. It is very important to us. We would definitely lose subscribers if those subscribers were able to see the services on a DIRECTV platform. We would be at a tremendous disadvantage.

Senator KOHL. Mr. Murdoch, let us say your sports programming is carried on the Fox TV network, which, as we have discussed, is not subject to your equal access promises, will you agree that for any sports programming, not now exclusive to DIRECTV, that you will still make it available to DIRECTV's competitors on non-discriminatory terms; for example, that the World Series will not be moved from Fox TV to DIRECTV exclusively?

Mr. MURDOCH. Absolutely, sir. I do not guarantee we will always have the World Series.

[Laughter.]

Mr. MURDOCH. The big problem, frankly, in all of this is the future of free broadcast. It is doubtful how long broadcast networks can keep paying for major sports.

Senator KOHL. Good.

Mr. MURDOCH. But that is another issue.

Senator KOHL. Thank you.

Mr. MURDOCH. It all leads to higher prices in cable. If they are going to insist on these prices, they are going to end up on cable networks, whether it is ESPN or a new competitor or someone, and it is going to force pricing to go up. There is a problem, and it has been the work of the marketplace—I am not complaining—but there is a problem because sports is just continually getting more expensive.

Chairman DEWINE. Senator Specter?

Senator SPECTER. Thank you very much, Mr. Chairman.

I would be surprised if my questions were not repetitious since I was unable to be here earlier, and this very distinguished panel has been testifying for the better part of an hour-and-a-half, interrupted by a vote.

Mr. Murdoch, permit me to begin with you. How many communications entities do you presently own?

Mr. MURDOCH. In this country, sir?

Senator SPECTER. No, take all of the countries.

Mr. MURDOCH. Let us start with this country, which is about 80 percent of our business. We own the Fox Network, and the Fox Movie Studios, and 30-odd television stations, local television stations. We also own the New York Post and Harper Collins book publishers.

In Britain, we own 2 daily newspapers and 2 Sunday newspapers. We have between 20 and 30 percent of the national market of newspapers there. We have a minority investment, such as we are talking about here, in BSkyB, a company I founded in order to challenge the established monopoly in Britain.

And then in Australia, we have some local newspapers, in Sydney, in Melbourne, Brisbane, Adelaide, and we have, if you look at our balance sheets, there are a lot of little things, but these are the main properties.

And then we have Star Television in Asia, which is a sort of long-term, start-up big—but we now are broadcasting 37 channels in 6 different languages across China, and India, and the Middle East, and Southeast Asia. They sound a lot, but they are relatively small business to the other things I have described.

Senator SPECTER. An obvious concern, Mr. Murdoch, with that much, by way of ownership, is the issue of concentration of power, which is always a concern, especially with the impact of the media on public opinion and political affairs. Do you consider that to be a legitimate concern?

Mr. MURDOCH. Not these days. I think there is such a multiplicity of voices everywhere that concentration is hardly possible. I mean, the most powerful, if you are talking about political influence, by far the most powerful company in this country is the New York Times, which services with its news just about every newspaper across the America, and is followed pretty slavishly by the 3 networks and its choice of news, but I am not saying that is bad or that it cannot be competed with.

You also have the Wall Street Journal, with a very large circulation, although it is a more specialized one. No, I think, if you look at the country as a whole, that is true. You can look at certain specific markets and say, hey, there is a large monopoly newspaper here and a large city with the number one television station and 5 radio stations, and huge cable interests in the rest of the country, and you can ask questions about that. But even in that case, I am sure there are, you know, there are suburban newspapers, and there are weeklies, and there are other voices.

Senator SPECTER. Mr. Murdoch, when you have—

Mr. MURDOCH. I would also say, if I may, Senator, that the power of the press is greatly overstated. We are much flattered by the interest of politicians, but—

Senator SPECTER. I do not think you will find anyone in the Senate who will agree with you about that.

[Laughter.]

Mr. MURDOCH. I am sure—or any politician anywhere in the world. But I have not noticed them change any election result yet.

Senator SPECTER. Well, that is because you have not been a candidate.

[Laughter.]

Senator SPECTER. Mr. Murdoch, when you have such a premier product such as the National Football League and the National Football Conference, and you have the Fox Network, and you have 30 TV stations, and you now seek to acquire a satellite, does that not put you in a position to charge pretty much what you want for rights to watch the National Football League?

Speaking as a long-time fan, I think that there are many people who would pay whatever it took to see the Philadelphia Eagles or the Washington Red Skins or the San Francisco 49ers play. And when you have the control of the transmission of those games, and then you have so many of your own stations you can play them on, and then you go to satellite as well, do you not think it is a fair concern that that concentration of power, with that kind of a product, gives you inordinate leverage to establish high prices?

Mr. MURDOCH. With respect, Senator Specter, no. It is the NFC, for which we pay \$550 million a year, is on free, over-the-air television, and there is a real question how long we can continue to pay such prices.

If you are talking about the NFL Sunday Ticket, which is on Direct and is exclusive, and which is also enormously expensive, that has been there for some time, and I understand there is a new contract for the next 4 or 5 years, but that has nothing to do with me, and it does not give us any power.

I better leave Mr. Hartenstein out of that because he is going to have to make it pay out.

Senator SPECTER. Mr. Kimmelman, what, in the last series of answers by Mr. Murdoch, do you agree with, if anything—

Mr. KIMMELMAN. Well, I agree when he said—

Senator SPECTER. —opposed to what you disagree with, but I thought we would start with a presumptively narrower arrange what you agree with.

Mr. KIMMELMAN. Yes, it is a short list. I definitely agree with Mr. Murdoch that there is a danger of concentration in local markets where you have monopoly newspapers buying the number one broadcast station, and I believe he is a bit understating dangers of concentration throughout markets.

And it is quite clear to me that, for example, in the Philadelphia market, being able to watch the Eagles is very important to consumers. And if my recollection is correct, when a cable company refused to sell its rights to sports programming, one of the satellite providers in the market found that only about half as many consumers were buying satellite service as in comparable communities in the country, reflecting the fact that they could not sell because consumers would not go where they did not get their local teams.

So it is an enormously powerful tool. It is market power at the programming level. I do not disagree with Mr. Murdoch that there is market power in the cable distribution system as well, but we are not serving consumers' interests when the 2 of them are fighting over monopoly rents, over overpricing, as opposed to competitive pricing, and that is the problem with this transaction.

It is shifting more power into the hands of one programmer who, with a new distribution system, has too much power in the marketplace to raise prices, not just to satellite customers, but to the other satellite provider and every cable operator because they are dependent on his product as a critical input to serve their customers.

Senator SPECTER. What is the additional factor, illustratively, of saying the New York Yankees, having their own cable, when you have the Atlanta Braves with their own cable outlet, and you have that in other forms, so that people want to watch the New York Yankees, and if you can only get it on cable, it drives up the prices?

This Antitrust Subcommittee I have been on for many years, and I commend the Chairman for these hearings, and we try to keep up with these issues, but they are vast, and they are complicated, and they overlap in so many, many directions. And one of the directions involves franchise shifts, and that involves enormous expense on stadiums.

In my State, Pennsylvania, we have seen 4 new stadiums built at a total cost in excess of right at a billion dollars, and those sta-

dium costs occur as a direct result of blackmail because those teams are going to go somewhere else or extortion.

I have a hard time being a Senator, but I have a pretty good command of blackmail and extortion from my prior practice. But how does the factor of—and that is a little different—but Mr. Murdoch would have a somewhat similar power with the NFL and people who want to see it—how does the factor of, say, the Yankees and their cable stations tie into this overall issue?

Mr. KIMMELMAN. Senator Specter, I think you are hitting a very important point because it would be appropriate for this Subcommittee to look at the leagues and their antitrust immunity under the Sports Broadcasting Act or under common law. That has been a problem that fuels this.

I would just point out that Mr. Murdoch is a team owner—the Dodgers, the Knicks, the Rangers, the Kings, the Lakers, Dodger Stadium—so he is part of that problem on that side as well. This is very, and I am not quibbling with his statement that he pays a lot, whether it is for his players or for his broadcast network, the right to televise games, but that is just institutionalizing overpayments, where the market itself knows there is not competitive pricing.

So there is lot of surgery that needs to be done, I would suggest, by the Congress to look at all levels of monopolistic practices, from the Leagues all through the sports broadcasting rights to the cable and satellite distribution systems.

Mr. CLELAND. Can I add a comment, Senator? Sports are an extraordinary example in the sense that they are like a personal monopoly. If you are a Yankees fan, you do not care to watch anybody else. You want to watch the Yankees. There is one choice. If you are Cincinnati Reds fan, you want to watch the Reds. And so it is our own personal loyalty to sports teams that creates a monopoly in that price.

Sports prices have gone up probably more than almost any other product in the economy over a long period of time. We remember when boxing used to be free on ABC Sports on Saturday afternoons. The reason it moved was because the business—they could earn a tremendous amount more money by doing it pay-per-view. And that is the trend, with Fox NFL, the NFL Ticket, that is the trend. They are realizing if they can constrain supply, they can leverage the personal monopoly of sports.

Mr. HARTENSTEIN. Senator, if I may, we have been on both sides of this. As you well know, in your State Comcast, to be very specific, has an ownership interest in both the Sixers and the Flyers and, through a loophole in the program access provisions, does not provide the Flyers or Sixers games to satellite. As Mr. Kimmelman indicated, we do not do as well in those territories where they are because we do not have the ability to deliver to our customers there those games.

On the flip side, in New York, with the Yankees being carried on the Yes Network, we made a promise to our customers long ago when we started, almost 9 years ago, that we would provide the regional sports network for their popular teams as part of our basic package to every customer. We bit the bullet. We did it. Cable, or

at least some cable in the New York area for the Yankees, did not and it has been very well publicized.

In neither case has this been the end of the world, and in all cases, as with NFL Sunday Ticket for us, at the end of the day it comes to consumers and what they are willing to pay.

Yes, we have Sunday Ticket, but the percentage of our total subscriber base that takes NFL Sunday Ticket is in the low teens. And it is just the market is a very efficient device in terms of prohibiting us or, for that matter, cable from over charging and gouging.

We have gone from zero to almost 12 million subscribers in 8 years. To some that is a damn good start. It is a textbook case in, I think, business school and I think Mr. Ergen at EchoStar would have a similar experience.

But at the end of the day, we are still only 12 percent of the homes in America, and we have a long way to go. I think this is all about competition, and what we are trying to do, and I think with News Corp. coming on board as a 34-percent owner, emphasis on 34 percent, is to be the innovator and extend the innovation and competitive alternative that we started. That is all that we are looking for, and I think that is what a lot of the folks are objecting about. They do not like competition.

Mr. MIRON. Senator, if I might, I think in respect to your original question about Philadelphia, at one point I think Mr. Murdoch was quoted as saying that sports were his, quote, "battering ram." And I think what we would be concerned about in Philadelphia is the retransmission consent that he might use in granting that, the ability to raise the price so that the Philadelphia Eagles would not be carried on a cable system and only on DIRECTV. And that would be part of what would—and if they were carried on cable, it would be because cable had to pay a higher price for that particular channel.

Senator SPECTER. Thank you.

Chairman DEWINE. Senator Leahy?

Mr. MURDOCH. Can I just add something to that? I am sorry, Senator. May I?

Chairman DEWINE. Mr. Murdoch, then Senator Leahy.

Mr. MURDOCH. I beg your pardon. I just want to—

Senator LEAHY. Senator Specter has asked a good question. I just did not hear your answer.

Chairman DEWINE. Go ahead.

Mr. MURDOCH. I wanted to say, reaffirm that the sports, which is always free bidding and free market, is carried on free television. We are totally 100 percent dependent on what advertising we get, and we are not about to give away 80 percent of the audience because we would lose 80 percent of our advertising, if not all of it. So it is just not a realistic thought to take it off cable.

Chairman DEWINE. Senator Leahy?

Senator LEAHY. I suppose I should be—have all my concerns and doubts put aside in this hearing, I don't. I saw the specter of nothing but nationally produced or geographically homogenized programming on satellite, indeed on cable, and I always worry about claims made. I voted against the—I was one of the few that voted against the Telecommunications Act. I really did not believe the claims that we would all see our cable bills come down. I think

mine has doubled or tripled since then. I really did not believe the claim that we would see much better, clearer TV. Most stations, if they are local, I can get a far better picture off rabbit ears than I can off my cable.

I was concerned about what many have talked about, that they will just use this—you go to like the so-called HDTV, just use all this extra spectrum to run ads and other businesses, not to give a better picture to the person buying it. But that is a different issue than here.

Now, though we hear reassuring pronouncements—and, again, I am concerned, and let me speak to a bit of a bias here. About a third of America lives in what could be called rural America. That is still a whole lot of people. That is about 90 million people. And in most of those areas of rural America, you do not get cable. You only get satellite, if you are going to get it, or over the air—you have to get it over the air somehow. A very important part of America. You cannot write off many million Americans, and you certainly, just as back in the days of Franklin Roosevelt, when a decision was made to bring electricity to rural America and telephones to rural America, to bring them into part of the country.

Now, I do not say that just coming from Vermont. We are basically very much a high-tech State. But every single Senator represents some large rural areas. In fact, I know from my childhood and visiting my uncle in Ohio, Senator DeWine has parts of rural Ohio which go way beyond what we think of as rural just because of the distances involved.

So that brings me to this. DIRECTV and News Corporation made public pronouncements about the hope of providing service outside large urban areas. I have not heard concrete plans to do so. To pick a State at random, say Vermont, what is the impediment to providing local-into-local TV today in Vermont, for example?

I mention this because EchoStar has done so. As I understand, when EchoStar did this, they courted a significant number of customers away from DIRECTV because you could get local programming. I would hope that that would provide an economic incentive for DIRECTV to do the same, but does anybody want to tell me, are they going to compete?

Mr. HARTENSTEIN. Sure, Senator. We have our eighth satellite, as I indicated, going up at the end of this year. It happens to be, while being our eighth satellite, our second spot beam satellite. We have not yet done the final testing to determine exactly how many additional markets and which ones in particular that we can cover. We know that we can take our total number of markets up to at least 100, and that will give us coverage of about 85 percent of the country.

We will, at the end of this year, which is not that much further away, have the ability to add some more markets, and we hope to be able to oblige at least the Burlington DMA, which is near about, if I understand or remember correctly, the 100th DMA. And so we—

Senator LEAHY. I think it is in the high 90's.

Mr. HARTENSTEIN. Yes, it is. So, we will look to that and see if it is technically feasible where exactly our spot beams fall. We come from different orbit locations.

Senator LEAHY. So, in other words, you have no—you are not saying there is—you are not making any commitment.

Mr. HARTENSTEIN. I cannot commit—

Senator LEAHY. Except to look at it.

Mr. HARTENSTEIN. I cannot commit specifically to Burlington today, but we are certainly looking at that and all the other markets that we might be able to cover. Our goal is to get to as many of the homes in America as we possibly can.

To answer your earlier question from your opening statement with respect to broadband, we today have a broadband service. It is called DIRECWAY, which works everywhere, including in all parts of Vermont, where by satellite—and it is a Hughes product—we can deliver high-speed broadband Internet via satellite, and we have a—

Senator LEAHY. Is that two-way?

Mr. HARTENSTEIN. Yes, it is two-way. Yes, sir.

Senator LEAHY. And is that comparable in price to cable broadband?

Mr. HARTENSTEIN. It is a little bit pricey right this minute. It will typically cost you about \$60 a month to get comparable service. But we have another service that should be launched by the middle of 2004. It is called SPACEWAY, also satellite-based but much higher performance, which will give much higher performance than even DSL or some cable modem service can today for a very similar price to what we are able to offer today.

Senator LEAHY. Am I right that in the service you have now, if there is suddenly a large demand, it slows down?

Mr. HARTENSTEIN. No, that is not correct.

Senator LEAHY. That is not correct. Okay.

Mr. HARTENSTEIN. I think you are thinking of cable or DSL there.

Senator LEAHY. I am familiar with cable and DSL, but I had heard that that happens on satellite. But not so?

Mr. HARTENSTEIN. Not the way we allocate the transponder capacity. No, sir.

Mr. CLELAND. Senator, could I add a comment on that with the rural satellite? It is going to be probably the only provider in some very rural spaces, but satellite will always be inferior as an architecture to a telephone or cable infrastructure because when you have to send signals on the IP protocol, you have to send up to the satellite and get answers. And so what it creates is a quarter-of-a-second delay because of the distance and bouncing back.

Now, for most services on high-speed, you would not notice the difference. For telephony you would. It would be like a bad walkie-talkie. If you were trying to do interactive gaming, like an F-15 fight with somebody across the country, it would be like flying a Sopwith Camel. So that is what the delay would be like.

Senator LEAHY. I am not very good at either the Sopwith Camel or the F-15, so I might be okay. However, my youngest son and daughter-in-law, who can fly such things, might feel differently.

We have been told that there would not be discrimination against unaffiliated programming services on DIRECTV. What about affiliated programming?



Mr. MURDOCH. Senator, we have made that quite clear. Any affiliated program would be treated exactly the same as a Fox program and a News Corp program. The misunderstanding here is, I think, that we amended our submission on this some weeks ago.

Senator LEAHY. Am I correct that that is if the FCC maintains its program access rules? Would you do that even if they did away with those program access rules?

Mr. MURDOCH. No, sir. We only ask for a level playing field. If they want to exempt all the cable companies and Time Warner with all their things, we would want the same treatment. All we ask for is the same treatment as cable gets.

Senator LEAHY. So if they did that, if they did away with program access rules, then as far as you are concerned, it is Nellie bar the door, just go ahead, and then you make the decision, whatever commitments are in place now would not be there—I am not trying to put words in your mouth.

Mr. MURDOCH. Our commitment is simply to extend the existing law from cable to satellite. The only person who will be exempt from it will be Mr. Ergen at EchoStar. We are happy with that.

Senator LEAHY. But if the FCC changes the program access rules, you would not feel that any commitment you made now stands? Is that right?

Mr. MURDOCH. I expect they would change it for everybody.

Mr. HARTENSTEIN. For the record, Senator, the program access rules were put in place in the 1992 Telecommunications Act as Mr. Kimmelman indicated, and the original sunset for those provisions was in 2002. They were extended for 5 years, so they are automatically now valid until 2007. And by our submission at the FCC, the joint News Corp./DIRECTV submission, we have voluntarily subjected ourselves to those exact terms.

Senator LEAHY. You subject yourself to FCC's non-discrimination principles by contract, correct?

Mr. HARTENSTEIN. Yes.

Senator LEAHY. How would you feel if that commitment was put into a consent decree by the Justice Department? Do you want to think that one over?

Mr. HARTENSTEIN. Well, if the program access rules were, again, applied to all MVPDs, vertically integrated ones, we would abide by those. Clearly, if there is a specific exclusion so that only DIRECTV would be subjected to those, I think that would be clearly an unlevel playing field against our MVPD competitors.

Senator LEAHY. But you are trying to get the Justice Department to go along with you. Still obviously there are certain give-and-takes when that is being done. You do not think this would be a fair one.

Mr. HARTENSTEIN. I think it would be—

Senator LEAHY. If they just put into a consent decree you have got to do this, even if the FCC later on changes their rules, which they seem willy-nilly able to do.

Mr. HARTENSTEIN. I think that would be unfair, yes.

Senator LEAHY. Mr. Murdoch, do you agree?

Mr. MURDOCH. I agree with Mr. Hartenstein, sir. We are simply seeking here the right to compete with cable on a level playing field, and all the submissions we have heard today are to try and

tie my hands behind my back from doing that. And if you want competition and service and price competition and everything to the public, I have to have the same privileges they have.

Senator LEAHY. I have never really pictured you as somebody with their hands tied behind their back with all—

Mr. MURDOCH. Well, that is the attempt that is going on here.

Senator LEAHY. It has usually been unsuccessful.

Does anybody want to add anything to this?

Mr. KIMMELMAN. Senator Leahy, I would just like to point out that I don't know where this level playing field is. Mr. Murdoch has a television network with Congressionally granted rights to get on every cable system in the country automatically. I know of no cable company that has such rights. I certainly believe cable companies that own their own programming can prefer their own programming and guarantee carriage on their systems. But there is something unique about a broadcast television network that Congress recognized and gave special privileges to.

So I am a bit baffled that Mr. Murdoch and Mr. Hartenstein are not willing to promise more, and particularly not promise more that covers not just cable programming but the broadcast programming to be offered on the same non-discrimination terms. It strikes me that they are unique by having a broadcast network and have through DIRECTV now a separate nationwide distribution system. No one else in the country is like that.

Senator LEAHY. Does anybody want to add to that?

Mr. MIRON. I was just going to say I support what Mr. Kimmelman said. The difference between—is definitely that News Corp would have a distribution, national distribution platform which no cable company has. The most a cable company has is a regional platform, and the greatest is to one-third of the country, but most of us much smaller.

Senator LEAHY. Well, Mr. Chairman, I will add my other questions for the record, and I appreciate we went over time on this. Thank you. I really enjoyed your football questions. We do not have those problems up in my little State.

Senator SPECTER. [Presiding.] Stick around. There are some more coming, Senator Leahy. Thank you very much to Senator Leahy.

Senator DeWine has stepped out for a few moments and has asked me to proceed at this time.

Focusing on the sports aspect, which may be the key point where so much or perhaps all of the other programming can be substituted for, but there is, as pointed out, only one New York Yankees, only one Philadelphia Eagles, only one Los Angeles Dodgers, when the Judiciary Committee has looked over these problems over the years, when we have had franchise transfers going back to the early 1980's and we had some very hotly contested hearings in this room when the Raiders moved to Los Angeles and Commissioner Rozelle was here with Al Davis and had about as lively a debate at that table as you can fathom. That was in 1982, and we have had the hearings periodically since. And there is always a question as to what Congress can do. And Congress probably does best when Congress does nothing. We have a lot of experience at that.

We do have tremendous leverage on the antitrust exemption, which baseball enjoys as a result of judicial decisions and which football enjoys as a result of legislation.

So if we were to insist on some other approach by Major League Baseball or by the NFL conditioned on losing their antitrust exemption, if they want to be like any other business—and we know baseball is a business at this point because the Supreme Court said so, long after the Holmes opinion in 1922, and we know football is a business, so that we could use that as leverage to structure some different arrangement. But then the question arises as to what arrangement would we suggest.

Mr. Cleland, starting with you, right to left, what would you say Congress ought to do to deal with this issue?

Mr. CLELAND. Try and offer a creative solution. I think the big problem from a Congressional standpoint is when consumers that might not way to pay for sports have to pay for sports. So probably one of the things is that as sports has migrated to pay-per-view, that has been a good development. But to the extent that sports costs are driving up, you know, cable programming and other programming, because they are bundled, you know, the technology nowadays allows you to select what programs you want. And you may have to buy 50, but you may only want three or five.

So I think, you know, any exploration of a la carte pricing from a Congressional standpoint would be something I imagine your constituents would like.

Senator SPECTER. Mr. Kimmelman?

Mr. KIMMELMAN. If I could echo that, we certainly would support moving towards a la carte pricing for consumers, pick the channels you want at a fair price, and I would suggest carrying it back into the wholesale level, each—

Senator SPECTER. At a fair price? How do you determine that?

Mr. KIMMELMAN. Well, if you can pick the channel you want at the retail level and you carry it back to the wholesale level and prohibit the bundling of channels so that they are sold to the distributor on an individual basis, you will get the closest you can to a market mechanism for people getting to choose what they want.

We have a problem with market prices here because we have cable monopolies; we have at best two satellite providers. It is an oligopoly structure. It is tricky.

I would urge you to review any antitrust immunity, first of all, for the leagues. I think it is problematic.

Senator SPECTER. Review it?

Mr. KIMMELMAN. And eliminate it.

Senator SPECTER. We have reviewed it again and again and again. But what do we put in its place? You talk about market. How do you get market for the New York Yankees television games, cable television games?

Mr. KIMMELMAN. If the Yankees are allowed to bargain on their own, you will see a very different result in the marketplace than if they are required to bargain through a league in a national package. You may need to look to special rules related to ownership of teams and ownership of distribution media. I think that creates problems.

As Mr. Cleland points out, this is a very tough set of issues because it has some inherent monopolistic aspects based on people's taste and also based on the fact that we have very few distribution mechanisms for televised sports, which is what people want. Certainly eliminating antitrust immunity would be a start, and requiring the sale of programming to all distributors on a per-channel basis and then to all consumers on a per-channel basis. People can bundle anything in addition to that.

Senator SPECTER. When you say eliminating the antitrust exemptions would be a start, would you recommend that we do that?

Mr. KIMMELMAN. Yes, sir, I do.

Senator SPECTER. What would happen? What would the consequence be? Would we not have a situation of chaos?

Mr. KIMMELMAN. We might have—we would have—we might have more chaos than we have today because leagues would not be able to organize how they maximize their profits for each of their teams. But you would certainly have the consumer able to pick and choose the teams he and she want to watch and see much more readily than you have today. You would not necessarily have certainty that teams would not move around. That is definitely a problem.

Senator SPECTER. Would we have teams? If you don't have the revenue-sharing of the NFL, would we have teams?

Mr. KIMMELMAN. We might have a lot more, Senator Specter. We might end up with more teams serving more communities, as you have in soccer in the U.K. Where we do not restrict exactly how the minor league is structured for baseball and major league is structured, you might have a much more open marketplace.

Senator SPECTER. Just let the market govern, no antitrust exemptions.

What do you think, Mr. Miron?

Mr. MIRON. Senator, I am not knowledgeable enough in this particular area to really try to—

Senator SPECTER. Well, don't let that stop you, Mr. Miron.

[Laughter.]

Senator SPECTER. Nobody else is either.

Mr. MIRON. I can only look at how legislation would affect us, and at this point I would not want to see Congress enact legislation that would force tiering or a la carte or any of that sort of stuff on a cable operator and a programmer. I would rather have us be able to enter into free market negotiations and continue to enter into negotiations, you know, with Fox Sports.

What I fear is that with the DIRECTV purchase, it would upset that free market negotiation. I think we have seen and we have seen now in New York a negotiation going on and some start towards the moving of cable programming, cable sports programming to a tier or something of that nature, and that to me—if we could have that free market negotiation and it could continue, maybe that has a way of helping it.

But I would be very cautious to ask the Congress to delve into that specific area because I think it would be very difficult.

Senator SPECTER. Mr. Hartenstein?

Mr. HARTENSTEIN. Senator Specter, I cannot speak for any given league, the NFL or any others, as to what their druthers are. But

I know in general programmers themselves do not like the notion of a la carte pricing or even tiering. It is terribly suppressive to the innovators who want to come up with new programming services. If everything went a la carte, the Animal Planets of the world, some of the new services just, I think, would be impossible to come into existence.

Senator SPECTER. Would that be bad?

Mr. HARTENSTEIN. Pardon?

Senator SPECTER. Would that be so bad?

Mr. HARTENSTEIN. Well, if you look at where people's choices were 10 years ago in terms of how many channels could a multi-channel programming provider provide, read cable 10 years ago, the answer was typically 30 or 50 or so channels. And while, yes, everybody only in their household professes to watch three channels, I tell you, if you get 50 households in a row, they will be a different three or nine or however many they watch in every one of those 50.

It is all about choice, sir, and I think that the cable industry has enough trouble answering the phone as it is. You know, trying to deal with customers wanting to change their a la carte lineup, I do not think they could handle it.

I think, quite frankly—that was a cheap shot, I know, Mr. Miron.

Senator SPECTER. How does DIRECTV do on answering the phone?

Mr. HARTENSTEIN. We do very well, sir. We are number one in both the ACSI and the J.D. Power independent customer satisfaction surveys. It is 2 years running now on ACSI.

Senator SPECTER. How does that compare to EchoStar?

Mr. HARTENSTEIN. EchoStar has come in number two, and the rest of the MVPD providers, cable, comes sort of a distant third.

Senator SPECTER. Judging by my cable company, you would not have to be very good to be better than they are.

[Laughter.]

Mr. HARTENSTEIN. Thank you.

Senator SPECTER. I say that very seriously.

Mr. Murdoch?

Mr. MURDOCH. Senator, I would just like to start by saying that I am pleased that Mr. Miron has just agreed to free market negotiations, which is just what we do.

On the bigger question of antitrust and the leagues, first of all, there seems to be some fiction that all these teams make a lot of money. I don't know any teams that make any money, particularly in baseball.

There is also the little fiction of Mr. Kimmelman's I might correct. We do not own Madison Square Garden or the Knicks or the Nets or whoever the hell are there. We do have a minority position in that, which we will be very happy if you ordered Cable Vision to give their money back. But we certainly have no influence at all on that.

The real point, we have just had this, as a matter of interest, in Europe and in Britain. We supported the start of a premier league in soccer and made it very popular, and it was a tremendous help to Sky Television, although it was very expensive. But it led to

huge improvement in football in Britain, and they share the money around.

Over the last year, the European Commission, Mr. Monti, the Commissioner for Competition Policy, has been driving at them to try and break it up and say this is monopolistic, it is a cartel, and so on. And he has finally backed away and given up on that and simply said they have to sell different packages of games.

But if you let each team negotiate for themselves, you are going to end up with half as many teams, not many more teams, as Mr. Kimmelman stated. The big teams will get all the money, and the little teams will get no money. And I think it would be very bad for the public and for the games. It would be better if Mr. Tagliabue of the NFL was here to articulate this rather than me. But I think the NFL has done a tremendous service to the public by controlling and sharing the money and sharing the talent equally.

It is a tricky problem. I know that sounds bad public policy, but it happens to work well in this case.

Senator SPECTER. Well, it certainly is a tricky problem, and it is extraordinarily difficult to try to find some answer, and Congress has shied away from it because of the lack of predictability of what would happen if we removed the antitrust exemptions. So we stumble along in what we are doing, and we really leave it up to the leagues. And I think baseball and football are getting into deeper trouble because you go to see the Philadelphia Eagles and you do not know any of the players. You go to see the Philadelphia Phillies and you do not know the players. Free agency has now put all the players on different teams. We had a lot of Philadelphia Eagles in the Super Bowl last year, but they were playing for Tampa or the other team.

Well, thank you very much, gentlemen. It has been very interesting and informative. Thank you.

Thank you, Mr. Chairman.

Chairman DEWINE. [Presiding.] Well, let me thank our witnesses for their testimony here today. As I stated at the outset, this transaction has important implications for pay-television consumers and for the media industry generally. And today's witnesses I think have really provided a great deal of information and insight into the issue, and we appreciate it.

Vertical transactions like the one before us today often raise very complicated competition policy issues, and I think it is fair to say that this deal certainly does that.

Senator Kohl and I continue to believe that the issues raised here today need to be thoroughly examined by the Justice Department and the FCC. And for that reason, we have sent a letter today to those agencies requesting that they review this deal carefully.

I would like to stress, however, that the Antitrust Subcommittee has not reached any conclusions about whether or not the deal should be approved. Similarly, we have not reached any conclusions as to the final form of any additional conditions which may be necessary.

We will issue, therefore, follow-up questions to today's witnesses, and we look forward to working with them as we continue to evaluate these important issues.

So, again, let me thank all of you very much for your patience and for your very good testimony. Thank you.

[Whereupon, at 4:52 p.m., the Subcommittee was adjourned.]

[Questions and answers and submissions for the record follow.]

## QUESTIONS AND ANSWERS

**Responses of Scott C. Cleland, CEO of The Precursor Group,  
to Post-Hearing Questions on the NewsCorp/DirecTV Deal from the Senate  
Subcommittee on Antitrust, Competition Policy, and Consumer Rights  
Hearing on June 18<sup>th</sup>, 2003**

**Answers to questions from Chairman Mike DeWine:**

1. Numerous commentators, such as MR. Kimmelman, have predicted that the News Corp./DIRECTV deal will result in higher prices for News Corp programming. If these commentators are correct, what effect, if any, do you believe that higher prices for NewsCorp programming will have on programming prices for other content? In other words, will higher prices for NewsCorp programming networks affect the prices for comparable networks?

**It is unlikely that NewsCorp has enough pricing power to move the entire industry in any particular direction. While NewsCorp has valuable programming, it does not completely set the bar for other content providers, such as Disney and Viacom, who have their own negotiating power to determine prices.**

2. Some of the media reports about this deal report that the Fox Entertainment Group ("Fox") portion of News Corp., in which DirecTV will be placed, took on about \$4.5 billion in debt – along with about \$225 million in interest expense – as part of this transactions.

Based on any experience you have analyzing acquisitions in this industry financed at least partly with debt, does Fox's debt, if the figures are correct, provide insight about the incentives of the merging parties to raise prices? What does this additional debt indicate about the potential of NewsCorp to raise programming prices?

**Higher programming prices obviously help FOX to handle its greater debt level since the company will have more revenue to cover interest payments or pay down debt. However, FOX is unlikely to see higher programming prices as the main driver to improving performance and thus, revenue. Instead, the success of DirecTV will largely depend on its ability to compete against cable—continuing to take market share and adding customers to cover the fixed costs of its network.**

3. In his testimony, Mr. Kimmelman suggested that Congress, among other things, "Let consumers pick the TV channels they want for a fair price" – essentially a suggestion for a la carte channel selection. What is your opinion of Mr. Kimmelman's suggestion and do you believe it is feasible?

**The market will likely continue to be the best method of determining fair price for programming content and the most effective means of delivery. A la carte programming is slowly becoming more and more a reality in the industry. The best example is the near complete move of boxing events to pay-per-view platforms. If**



**consumers see a value and are willing to pay for it, more content will likely be moved to an “on-demand” pricing model.**

4. Some concerns have been raised that Fox Owned and Operated television stations will not negotiate aggressively with DIRECTV for retransmission compensation once this deal is complete.

Do you believe this deal will alter the negotiations between Fox Owned and Operated stations and DirecTV for retransmission consent? If so, do you believe the changes in the negotiations between Fox Owned and Operated television stations and DirecTV will affect the retransmission consent negotiations between DirecTV and Fox affiliate stations? How do you believe those negotiations will be affected?

**It is possible that it will affect negotiations on the margin, but changes are unlikely to be in the realm of anti-competitive behavior.**

**Responses of Scott C. Cleland, CEO of The Precursor Group,  
to Post-Hearing Questions on the NewsCorp/DirecTV Deal from the Senate  
Subcommittee on Antitrust, Competition Policy, and Consumer Rights  
Hearing on June 18<sup>th</sup>, 2003**

**Answers to questions from Senator Herb Kohl:**

1. Are there any conditions do you believe the Justice Department and/or the FCC should place upon approval of the News Corporation/DIRECTV transaction? If so, what are they?

**No. This merger is not anti-competitive, and conditions on mergers are generally only appropriate in very special circumstances.**

2. Many believe that this deal will lead other media companies seeking to acquire cable or satellite companies. Do you think that this deal will inevitably set in motion a chain of media content/distribution mergers? What type of deals do you think are likely?

**More consolidation in the industry is likely. EchoStar is likely to be eventually acquired. However, the impetus for consolidation is not the NewsCorp/DirecTV deal, but the increasing threat of digitization on the value of content. Content is under siege from growing piracy from Napster-like file sharing and from ad zapping via Tivo-like technology. Broadcasters need to find a secure network (either cable or DBS) to transmit their content in order to retain its value. NewsCorp understands this and has sought protection through the acquisition of DirecTV. Disney and/or Viacom are likely to follow a similar path in the future.**

3. (a) News Corporation has promised that any "related party" transaction between NewsCorp and DIRECTV must be approved by the audit committee of Hughes Electronics, made up of independent directors. News Corporation argues that this should safeguard against "sweetheart deals" between News Corporation and DIRECTV. However, many have criticized this arrangement as ineffective, including Professor Stout of the UCLA Law School. She says in her submission to the FCC that audit committees aren't used for this purpose. What's your view of this arrangement? Do you believe that this audit committee will truly be an independent watchdog to prevent sweetheart deals? If not, can you think of any other mechanism to address self-dealing between News Corporation and DIRECTV?

**Establishing an audit committee is a new mechanism following the Sarbanes-Oxley Act of 2002. The audit committee is a legitimate experiment in trying to prevent "sweetheart" deals, providing a viable "paper trail" to examine such deals.**

- (b) Can you recall any other situation in which an independent audit committee has been used in a similar circumstance? If so, please specify.

**No -- not under the same conditions.**

4. Do you believe that News Corporation is likely to buy a majority stake in Hughes once its commitment not to buy more expires? Would doing so advantage News Corporation in any respect?

**Since NewsCorp has effective control, greater investment is not necessary. However, NewsCorp may decide to increase its stake for financial or other reasons at a later date.**

5. In your opinion, will the Audit Committee of Hughes be a sufficient protection against "sweetheart" deals and self-dealing between News Corporation and Hughes if News Corporation acquires a majority interest in Hughes, or acquires 100% of Hughes? Why or why not?

**The audit process will likely have a disruptive effect on "sweetheart" deals since it establishes an additional process and creates a "paper trail", which can be checked and followed to ensure arms length transactions.**

ANSWERS OF EDDY HARTENSTEIN, CHAIRMAN AND CEO, DIRECTV, INC.,  
TO FOLLOW-UP QUESTIONS POSED BY SENATOR DEWINE

1. One of the major potential benefits of this deal is News Corp.'s pledge to expand DIRECTV's "local into local" service well beyond the 100 DMAs planned by DIRECTV. Increased local into local was also supposed to be one of the benefits of the EchoStar/DIRECTV deal. At the Antitrust Subcommittee hearing on the EchoStar/DIRECTV merger, you said "Neither DIRECTV nor DISH Network alone has sufficient spectrum to provide all local channels, as well as the national pay cable networks to viewers in every one of the country's 210 local-channel markets." You went on to say that without the EchoStar/DIRECTV merger, residents of communities such as Rhinelander, Wisconsin, the 137<sup>th</sup> DMA and Zanesville, Ohio, the 202<sup>nd</sup> DMA, were unlikely to see satellite delivered local channels "in our lifetime."

**(a) Q: Only 15 months have passed since you made those statements. Do you now believe that News Corp./DIRECTV combination could enable local into local in all 210 markets?**

*A: As my statement 15 months ago indicated, providing satellite-delivered local broadcast channels to all 210 DMAs is an enormous technical and economic challenge. DIRECTV has already announced its intention to expand local-into-local service to more than 100 DMAs upon the successful launch of its new DIRECTV 7S spot beam satellite in the fourth quarter of this year. The pace and scope of local-into-local expansion beyond that is difficult to predict, in particular because the transaction will not result in any spectrum gain. As you know, News Corp. was the first company to propose the delivery of local broadcast channels via DBS in the late 1990s, and continues to be a strong supporter of that concept. News Corp. has indicated that expansion of local-into-local service will be a top priority if its proposed investment in Hughes receives government approval.*

*I would add that, as compared with our current situation, the improved capital structure of Hughes and DIRECTV after the transaction with News Corp is consummated will put DIRECTV in the best possible position to meet the challenge of serving all 210 DMAs with satellite-delivered local broadcast channels.*

**(b) Q: Are there any other potential business arrangements that would also allow DIRECTV to expand its local-into-local service offering beyond the planned 100 DMAs?**

*A: We have explored all business options available to us to address the technical and economic challenges involved in moving beyond the more than 100 DMAs that we will serve upon the successful launch of DIRECTV 7S. Today, we do not believe that any business arrangement other than the transaction with News Corp. holds any realistic prospect of significantly enhancing DIRECTV's ability to expand local-into-local service.*

ANSWERS OF EDDY HARTENSTEIN, CHAIRMAN AND CEO, DIRECTV, INC.,  
TO FOLLOUP QUESTIONS POSED BY SENATOR KOHL

1. Last year, when we considered EchoStar's proposal to acquire DIRECTV, one [of] the asserted benefits was that the combined company would commit to provide local broadcast signals to all 210 markets across the nation. Right now, DIRECTV offers this "local-into-local" service into about 60 markets, but has pledged to expand this service into the 100 largest markets by the end of the year. I believe local-into-local service is essential to make satellite a viable competitor to cable.

**(a) Q:** As you know, News Corporation has committed to "explore the feasibility of aggressively expanding DIRECTV's local-into-local service" once this transaction is completed. What does this mean? Can you be more specific with respect to expanding the number of markets to which DIRECTV will bring local-into-local service, and the dates by which you will reach such targets? Will you agree to make these commitments a condition of approval of your deal?

*A: Providing satellite-delivered local broadcast channels to all 210 DMAs is an enormous technical and economic challenge. DIRECTV has already announced its intention to expand local-into-local service to more than 100 DMAs upon the successful launch of its new DIRECTV 7S spot beam satellite in the fourth quarter of this year. The pace and scope of local-into-local expansion beyond that is difficult to predict. As you know, News Corp. was the first company to propose the delivery of local broadcast channels via DBS in the late 1990s, and continues to be a strong supporter of that concept. News Corp. has indicated that expansion of local-into-local service will be a top priority if its proposed investment in Hughes receives government approval.*

*I would add that, as compared with our current situation, the improved capital structure of Hughes and DIRECTV after the transaction with News Corp is consummated will put DIRECTV in the best possible position to meet the challenge of serving all 210 DMAs with satellite-delivered local broadcast channels.*

*Finally, we do not think it would be appropriate to condition approval of the transaction on the commitment to a specific timetable for the initiation of local-into-local service in particular markets.*

**(b) Q:** Will DIRECTV also agree to offer broadband services to rural communities by specific dates in the future? Please describe how many communities will be covered by this commitment, and by what date.

*A: Although DIRECTV currently does not offer broadband services to its subscribers, its sister company, Hughes Network Systems ("HNS"), does offer its DIRECWAY two-way satellite Internet service nationwide, including in rural communities. HNS has pioneered the development of satellite broadband services. News Corp. has indicated its intention to explore partnering with other broadband providers, including those offering satellite broadband, DSL, and new Wi-Fi services. News Corp. believes, and we agree, that it is important for consumers*

*to have a vibrant set of broadband choices that compete with cable's video and broadband services on capability, quality and price.*

*Finally, we do not think it would be appropriate to condition approval of the transaction on the commitment to a specific timetable for broadband services.*

**2.(a) Q: News Corporation has promised that any "related party" transaction between News Corp. and DIRECTV must be approved by the Audit Committee of Hughes Electronics, made up of independent directors. News Corporation argues that this should safeguard against "sweetheart deals" between News Corporation and DIRECTV. However, many have criticized this arrangement as ineffective, including Professor Stout of UCLA Law School. She says in her submission to the FCC that Audit Committees aren't used for this purpose. How can we be satisfied that this Audit Committee will truly be an independent watchdog to prevent sweetheart deals? As the current CEO of DIRECTV, are you satisfied that this Audit Committee will sufficiently protect the interests of DIRECTV with respect to transactions between News Corporation and DIRECTV?**

*A: I am completely satisfied that the interests of DIRECTV will be protected with respect to transactions between DIRECTV and News Corp. for a number of reasons. First and foremost, we have a team of experienced and motivated employees at DIRECTV who are proud of the business they've created. They are compensated, in significant part, based on DIRECTV's performance, but more importantly they are committed to our business and our customers. Hughes and its shareholders (including News Corp. when this transaction is completed) will best be served by strengthening the DIRECTV employee commitment to its business and customers, not by attempting to impose "sweetheart deals."*

*Second, the Hughes Audit Committee will certainly support DIRECTV's management and employees in assuring that the interests of DIRECTV will be protected in transactions with News Corp. and its affiliated companies. The Audit Committee will be comprised entirely of independent directors. This will be required by our charter and is consistent with pending listing standards of the New York Stock Exchange (NYSE), where Hughes will be listed. The NYSE has indicated that it believes audit committees made up of independent directors are "particularly well suited" to review related party transactions. Third, Hughes' by-laws will provide the Audit Committee with the ability to retain experts to assist in its review of transactions between News Corp. and DIRECTV. Further, our directors, including those who serve on the Audit Committee, have fiduciary obligations to all of Hughes' stockholders. Breaches of these obligations could result in personal liability on the part of the directors who serve on the Audit Committee. With this in mind, when in doubt I presume these directors will retain experts to assist them in their review of transactions with News Corporation. In this era of enormous sensitivity to the responsibilities of independent directors, and with the specter of personal liability present, I have no doubt that the independent directors serving on the Audit Committee will take their responsibilities very seriously.*

*In addition, any self-dealing transaction with News Corp. which is unfair to Hughes could result in liability of News Corp. to the other shareholders of Hughes. As a public company, Hughes*

*will be required to publicly disclose any material affiliate transactions, so there will be no secret dealings. Class action plaintiffs' attorneys, who are incentivized by contingent attorney's fees, can be expected to bring lawsuits against News Corp. challenging the fairness of any apparent "sweetheart deal". Therefore, I believe that News Corp. would be hesitant to engage in a "sweetheart deal" even in the absence of the Audit Committee protection.*

*Moreover, as explained in the statements we filed with the FCC by some of the nation's preeminent economists, DIRECTV has insufficient power in the MVPD market, and News Corp. has insufficient power in the programming market, to make foreclosure strategies involving withholding programming or raising the price of such programming profitable, so the "sweetheart" deal scenario hypothesized is, as a matter of economics, simply unlikely to occur in the real world. We have attached copies of these expert statements, along with our Opposition to Petitions to Deny and Reply Comments, which address this issue at length.*

*Finally, DIRECTV has about \$3 billion in indebtedness which is governed by agreements that require that related party transactions be on an arm's length basis and impose review and independent evaluation for material transactions of this type. With so much at stake, it is hard to imagine that News Corp. would attempt to engage in transactions that are unfair to DIRECTV.*

*I also would note that Professor Lawrence Hamermesh of Widener University has submitted an affidavit to the FCC (also attached) which explains that Professor Stout's observations are based on inaccurate information and erroneous on a number of important points.*

**(b) Q: How will the functioning of the Audit Committee change if News Corporation in the future purchases a majority share of Hughes Electronics? Specifically, will the Audit Committee continue to function and be constituted entirely by independent directors if News Corporation purchases a majority of Hughes, or if it purchases 100% of Hughes?**

*A: I know of no plans by News Corp. to acquire a majority ownership stake in Hughes. My understanding is that as long as Hughes Electronics remains publicly traded on the New York Stock Exchange, the independent director composition of the Audit Committee will remain the same, and the various considerations I have mentioned above also still will apply so long as Hughes has other shareholders besides News Corp. and its affiliates or has indebtedness with restrictions on non-arm's length transactions. More fundamentally, however, the FCC would have to approve any transaction in which News Corp. attempted to acquire more than 49.9% of Hughes shares.*

**(c) Q: At the hearing, Rupert Murdoch states that it would be impossible for News Corp. to impose supra-competitive programming price increases on DIRECTV because News Corporation will own only a 34% stake in Hughes, and any such price increases would have to be approved by the Hughes Audit Committee. Will the Audit Committee continue to serve as an independent safeguard on News Corporation's ability to impose programming price increases on DIRECTV if News Corporation obtains a majority stake in Hughes, or if News Corporation purchases 100% of Hughes? If your answer is affirmative, explain why.**

*A: As mentioned above, the Audit Committee would continue to be comprised entirely of independent directors even if News Corp. acquired a majority interest in Hughes, assuming that Hughes Electronics were to remain publicly traded on the New York Stock Exchange, and the various considerations I have mentioned above also still will apply so long as Hughes has other shareholders besides News Corp. and its affiliates or has indebtedness with restrictions on non-arm's length transactions. More fundamentally, however, the FCC would have to approve any transaction in which News Corp. attempted to acquire more than 49.9% of Hughes shares.*



July 14, 2003

**Robert Miron's Answers to  
Senator Mike DeWine's Follow-up Questions  
"The News Corp./DirecTV Deal:  
The Marriage of Content and Global Distribution"  
Hearing on June 18, 2003**

1. We will respond as we have in the past, by improving our own offerings. DBS competition is certainly one reason, among others, that the cable industry has invested so substantially in recent years in upgrading its plant and expanding its programming offerings. Since 1996 cable operators have invested more than \$70 billion in improving plant and equipment, and over the same period, spending on programming has nearly doubled. We are already committed to adding interactive features to our programming, and to supporting HDTV. If, as Mr. Murdoch testified, DirecTV places increased priority on these areas, that will place us under even greater pressure to perform, and consumers will benefit.

2. (a) We believe the acquisition will give News Corp. substantial additional leverage in negotiations because a temporary interruption of service would, as you point out, confer substantial benefits on DirecTV. This means that the power of News Corp. to ask for more will increase dramatically, and the power of cable to resist will decrease. Whether this causes more service interruptions, or whether there will be fewer because of the cable industry's reduced power to resist, is unclear to us. What is clear is that the final result will be higher prices to both cable and DBS customers.

(b) As we said in the previous response, the answer to this question is not clear to us. It may be that disputes will actually be shorter; it may be that they will be longer. But the impact on consumers is clear to us – the alteration in the existing balance of power will result in higher consumer prices for cable and DBS.

(c) Now, when tough negotiations for retransmission consent or cable network carriage result in a service interruption, both the network and the cable operator are hurt. The News Corp. broadcaster or cable network loses advertising revenue, and the cable system loses customers to DirecTV and EchoStar. Networks negotiate retransmission consent for the entirety of their owned and operated stations, and they negotiate with cable operators on a company-wide basis. News Corp., with stations in nine of the top ten markets and sixteen of the top twenty, already has leverage to inflate programming costs nationwide. Acquisition of DirecTV will shift the leverage point much further in favor of News Corp., because in return for the temporary loss of advertising revenue, they will achieve both higher programming prices and the economic benefit of permanent additions to DirecTV's customer base.

3. (a) Rising programming costs (including costs associated with retransmission consent) are a major factor in the cost of cable to consumers. There is no doubt that increased costs for News Corp. programming, resulting from the additional leverage from acquisition of DirecTV, will be reflected in cable rates.

Miron Answers to DeWine Questions  
July 14, 2003  
Page Two

(b) If News Corp. follows through with its commitments to invest in DirecTV, that will put additional pressure on the cable industry to increase our already substantial investment in technology and service upgrades.

4. In general, we do not believe this transaction impacts the bargaining power of other programmers. However if, as is likely, News Corp. were to use its increased strength to bid up the price of sports programming even further, other networks would be under pressure to bid up as well, and to pass through their increased costs to cable operators and cable customers. Sports programming is already by far the largest component of programming cost increase; this already alarming trend could be accelerated. In addition, we believe that one of the three other network companies is likely to link up with EchoStar, to equal the advantages News Corp. will gain by acquiring DirecTV. This would multiply the adverse effects of the News Corp./DirecTV transaction.

5. As a general proposition, we do not believe that a dramatic shift to a la carte pricing of programming now carried in the "expanded basic" package of services is feasible. First, we believe consumers would not find the a la carte approach attractive. Second, a la carte carriage is prevented by virtually all contracts between cable systems and programmers; this contractual web would be virtually impossible to unweave. Third, programmers have based their entire business plans on the expanded basic tier. The damage to them in radically altering existing carriage patterns would be severe. On the other hand, one reason that the expanded basic tier continues to grow is that the broadcast network companies use their retransmission consent leverage to keep their affiliated cable networks on the expanded basic tier, and to place new networks there. News Corp.'s acquisition of DirecTV, for example, will make it much harder for cable operators to encourage Fox regional sports networks, which grow ever more expensive, to move out of expanded basic and into optional tiers of service.

July 14, 2003

**Robert Miron's Answers to  
Senator Herb Kohl's Follow-up Questions  
for News Corp./DirecTV Merger Hearing**

1. Our group of four companies is working on the question. Over the course of the FCC and Justice Department review of this transaction, we will be making specific recommendations, and we will be happy to submit them to you at that time.

2. Advance/Newhouse is a privately held company. We are happy with the extent of our holdings, and we would be unlikely to consider such a move. I doubt, though, that we would get such an offer. Ever since retransmission consent was adopted in 1992, the general trend has been toward affiliation of programmers with network broadcasting companies, and away from affiliation of programmers with cable system operating companies. Of the five major multichannel program suppliers only one, AOL Time Warner, is cable system-affiliated and that affiliation predates the 1992 Act. I do not believe that programming companies would want to acquire small cable companies, or larger cable companies for that matter, because broadcast affiliation is now the key element. I do believe that, because News Corp. will be uniquely advantaged as the only broadcast company affiliated with a national distributor, it is likely that one of the three remaining network broadcasters will seek to affiliate with EchoStar.

3. I am not challenging News Corp.'s good faith. Moreover, they have offered to make their commitments enforceable by consent decree. I am concerned that News Corp.'s commitments do not cover broadcast retransmission consent negotiations at all, and that even with respect to their satellite programming, the commitments allow them to raise prices so long as they do so to all three platforms—cable, DirecTV and EchoStar.

FOLLOW-UP QUESTIONS TO RUPERT MURDOCH  
 “THE NEWS CORP./DIRECTV DEAL:  
 THE MARRIAGE OF CONTENT AND GLOBAL DISTRIBUTION”  
 HEARING ON JUNE 18, 2003

QUESTIONS OF CHAIRMAN DEWINE

1. *You have testified that “News Corp. is committed to dramatically increasing DIRECTV’S present local-into-local commitment of 100 DMAs by providing local-into-local service in as many of the 210 DMAs as possible, and to do so as soon as economically and technologically feasible.” Can you assure the Subcommittee that you can and will provide local-into-local in more local markets than DIRECTV can now?*

*Please provide specific details about News Corporation’s (“News Corp.”) commitment. In your answer, please include the following information:*

- a) News Corp.’s current projection or “best guess” of the total number of DMAs into which it will provide local-into-local service;*
- b) News Corp.’s estimated time for providing local-into-local into the total number of DMAs that it currently projects providing local-into-local service;*
- c) When will News Corp. consider its commitment to offer local-into-local into a DMA fulfilled – once local-into-local service is offered in any portion of the DMA, or only once local-into-local is offered in the entire DMA? If News Corp. will consider its commitment fulfilled once it offers local-into-local in any portion of a DMA, please explain how News Corp. will determine which areas within a DMA will receive local-into-local and which areas will not receive it.*
- d) The factors that will guide News Corp. in determining whether it is “technologically and economically feasible” to provide local-into-local service into a DMA.*

As you correctly note, News Corp. is committed to providing local-into-local service in as many of the 210 DMAs as possible, and to do so as soon as economically and technologically feasible. We can certainly commit to providing local-into-local service in *more* local markets than DIRECTV currently anticipates. We can also point to News Corp.’s historical and ongoing commitment to local-into-local service, both when it first proposed DBS local-into-local as the owner of the ASkyB DBS venture, and as a longstanding broadcaster with a strong belief in and commitment to local broadcasting. From a competitive perspective, News Corp. is also motivated by its desire that DIRECTV be an ever-stronger competitor to cable and EchoStar, which is also aggressively rolling out local-into-local service.

Toward this end, News Corp. is actively exploring various options for accomplishing local-into-local in as many DMAs as possible. Once News Corp. has explored the various options for

providing these services, it will be in a better position to provide additional details about its plans for rolling out additional local-into-local service. However, such details are currently unavailable and are dependent on such unknown variables as the costs associated with launching additional satellites and backhaul facilities, transponder capacity and future advances in compression technology. Additionally, News Corp. is exploring whether current DIRECTV controlled satellite slots could be rededicated to local-into-local from other current purposes.

2. *What, if any, additional investments must News Corp. make, in terms of additional satellites or other investments, in order to deploy local-into-local in all 210 DMAs?*
  - a) *Will you commit to make the investments necessary in order to provide local-into-local in all 210 DMAs?*
3. *Some have proposed conditioning this transaction upon commitment to carry local into local in all 210 markets by a set date. Would this be an acceptable condition to News Corp.?*

Unfortunately such a condition would not be in the public interest, nor would it be feasible at this time. As the FCC recognized just last October, the pace of technological improvements necessary to make such service feasible in all 210 DMAs is "difficult to predict." *EchoStar/Hughes*, 17 FCC Rcd. 20559, 20595 (2002). Therefore, any specific deadline imposed would of necessity be somewhat arbitrary. Such a condition could threaten the viability of DIRECTV if it proved in the future to be economically or technically infeasible to provide local-into-local service to 210 DMAs, or to do so pursuant to an arbitrary, unrealistic time frame. The Subcommittee can rest assured, however, that News Corp. is highly motivated, for the reasons set forth above, to provide local-into-local service in as many DMAs as possible.

4. *In testimony to the House Judiciary Committee you stated that you "intend to approach Mr. Ergen and see if we can't share some of the costs" associated with uplinking broadcast signals to satellite in order to expand the availability of those signals, especially in rural areas. Concerns have been raised that such collaboration between EchoStar and DIRECTV would entrench those incumbent DBS providers. Are you willing to commit to allow any DBS provider, including new entrants, the opportunity to participate in such a cost sharing agreement, on reasonable terms, in order to expand the availability of local broadcast service in rural areas?*

News Corp. is willing to commit to discussing with any new DBS entrants such a cost sharing agreement on reasonable terms. Any agreement to *reduce* the cost of providing local-into-local service would be commercially and economically in DIRECTV's best interests.

5. *In the dispute between Cablevision and the YES network, which owns the rights to carry Yankees and New Jersey Nets games, the parties could not agree on carriage terms, so Cablevision did not carry Yankees and Nets games. DIRECTV, which did carry the games, increased subscribership as much as 186% in Cablevision zip codes compared to 6% in other zip codes, according to some reports.*

*News Corp. owns many regional sports networks that broadcast the games of local sports teams. According to the New York Times story cited by Mr. Kimmelman, Fox's Regional Sports Networks ("RSNs") control the regional broadcast rights to 67 out of 80 professional basketball, hockey, and baseball teams. Fox has had disputes similar to the Cablevision/YES dispute with Time Warner cable in Minnesota and Florida. In the past, the fact that both the cable system and the cable network were suffering some economic damage meant that they both had strong incentives to reach a settlement. If News Corp. owns DIRECTV it will be in a position to reap some gains from the dispute – its losses from loss of carriage on the cable system will be at least somewhat mitigated by gains in its DIRECTV business.*

*Will News Corp.'s ownership of DIRECTV affect the likelihood that there will be more disputes between News Corp. and cable companies over price or conditions of carriage?*

*a) Do you believe News Corp.'s ownership of DIRECTV will affect the length of any disputes between News Corp. and cable companies that occur over carriage of News Corp. programming?*

The Joint Reply and CRA Report contain detailed analyses and explanations as to why it would not be in News Corp.'s economic interest to lose distribution of its programming on competing platforms (whether cable or EchoStar) in an attempt to induce consumers to switch to DIRECTV (Joint Reply at 27-36; CRA Report at 26-43; 47-50). Sound economic theory demonstrates that a strategy to foreclose competitors' access to News Corp. programming, either by withholding programming completely or by a uniform price increase, would cause News Corp. to lose more money on its programming assets than it could possibly gain through its share of DIRECTV. Even the loss of highly popular programming does not create the subscriber movements or support price increases of the magnitude that would be required to make such a foreclosure strategy profitable for News Corp. The "reported" statistics concerning the YES Network dispute cited above are not accurate. As we point out in the Joint Reply, Cablevision lost no more than 1% of its overall subscriber base in the New York region during the entire year when it did not carry the YES Network. (Joint Reply at 29; see also CRA Report at 37) Conversely, DIRECTV's subscriber count in the region increased by only a few percentage points – nowhere close to the 186% mentioned in the reports you cite and far below the level that would be necessary to make a foreclosure strategy profitable even if all DIRECTV's growth were attributable to the "YES factor."

News Corp. depends on cable and EchoStar for over 85% of the distribution of its programming networks. It is not in our interest to have disputes of any kind or of any duration with our distribution partners. It is in our interest to reach mutually acceptable carriage arrangements with all distributors with no interruption of service to consumers. These interests will not change if News Corp. owns a 34% interest in Hughes/DIRECTV.

*6. Some of the media reports about this deal report that the Fox Entertainment Group ("Fox") portion of News Corp., in which DirecTV will be placed, took on about \$4.5 billion in debt – along with \$225 million in interest expense – as part of this*

*transaction. At least one stock analyst downgraded her recommendation on Fox stock reportedly because of this extra debt.*

- a) *Are the cited figures correct?*
- b) *Does the extra debt and resulting interest expense mean that News Corp. will face pressure to increase programming prices to cover that additional expense?*

The cited figures are correct. Please note, however, that this indebtedness is owed by Fox to News Corp., which is funding the purchase of Hughes shares through the use of its own cash and securities. Fox will be more than able to cover its increased debt service expenses using its free cash flow and will not in any way be required to increase programming fees in order to meet its financial obligations.

- 7. *News Corp. owns many highly popular cable networks, including Fox News Channel and many RSNs. You have pledged to make News Corp.'s cable networks available on non-discriminatory terms. Mr. Kimmelman and others have raised concerns, however, that this pledge still leaves News Corp. free to raise prices to cable systems and to EchoStar, as long as it raises the price to DIRECTV as well.*
  - a) *Will any of News Corp.'s non-discrimination pledges prevent it from raising prices, by equal amounts, to cable companies, EchoStar, and DIRECTV?*
  - b) *Do News Corp.'s pledges mean, in effect, that the terms of any agreements on price and other carriage provisions between News Corp. and cable companies and EchoStar will track terms of agreements reached between News Corp. and DIRECTV? If not, please explain how News Corp. will ensure that it offers its programming services "to all MVPDs on non-exclusive basis and non-discriminatory terms and conditions" as it has committed to do.*

The Joint Reply and accompanying economist reports explain why, regardless of the FCC's program access requirements and the News Corp./DIRECTV program access commitments, it would be economically irrational for News Corp. to pursue a uniform price increase strategy. (Joint Reply at 32-35, 38-44; CRA Report at 57-62; Lexecon Report at 25-27). Such a strategy would be unprofitable for a number of reasons, which are enumerated in the Joint Reply and accompanying reports. Even if the conclusions of our expert economists are wrong and a uniform price increase strategy were both possible and profitable, the FCC's program access rules and the parties' program access pledges act as an *additional* constraint on anti-competitive or discriminatory actions by both News Corp. and DIRECTV.

The FCC's program access rules currently apply to all of News Corp.'s cable programming services. The News Corp./DIRECTV program access undertakings go further than the FCC's rules, because they not only constrain News Corp. and DIRECTV with respect to our own programming services, but also constrain us with respect to programmers that hold an interest in either company, such as Liberty Media. Thus, News Corp. and DIRECTV have agreed to abide

by restrictions that are *more onerous than the restrictions that apply to AOL/Time Warner, AT&T/Comcast, Cox or any other vertically integrated cable operator/programmer*. The FCC has consistently concluded that the program access rules are effective to prevent anti-competitive abuses (Joint Reply at 61; Consolidated Application at 59). If News Corp. fails to adhere to the rules, the FCC has a carefully-crafted complaint procedure that aggrieved parties can utilize. Since we have asked the FCC to make compliance with program access commitments a condition of the grant of the DIRECTV license transfer to News Corp., we violate those rules and undertakings at our peril. We therefore believe that the FCC's rules and our program access commitments provide more than adequate protection to competing programmers and distributors.

8. *The FCC has previously calculated that new programming networks need access to approximately 20% of all MVPD subscribers in order to become viable. According to the last FCC report on competition in the video marketplace, about 12% of all MVPD subscribers subscribe to DIRECTV. To the extent that they access to DIRECTV subscribers, new Fox programming networks may have an advantage in reaching the number of subscribers necessary to attain viability.*
- a) *If this deal is approved, do you anticipate launching additional Fox networks?*
  - b) *Will the acquisition of DIRECTV affect News Corp.'s analysis of whether to launch new programming networks? How?*
  - c) *Briefly outline the analysis that News Corp. undertakes when deciding whether to launch new programming networks.*

Fox Cable Networks currently has no plans to launch additional cable networks, other than ("Fuel," an extreme sports channel) it is currently in the process of launching. The acquisition of DIRECTV will not affect News Corp.'s analysis of whether to launch new programming networks for two reasons. First, as your question recognizes, DIRECTV represents only about 13% of all MVPD subscribers, and a new programming network needs access to *at least 20%* of all MVPD subscribers in order to become *viable* (and in Fox's view, the number of homes needed to become commercially *successful* is 30-35 million homes (or approximately 33-40% of all MVPD subscribers), as this is the number of homes needed to attract national advertising). Thus, access to DIRECTV alone would not ensure the viability of a new programming network. Second, News Corp. has historically had a good record of securing carriage of new channels on DIRECTV, even in the absence of any economic stake in that company, because DIRECTV has a greater number of channels to program than do many cable operators. Moreover, because of the procedures in place to oversee related party transactions, any proposals to launch new Fox programming networks would be closely scrutinized, at arms length, by Hughes' Audit Committee. (See Joint Reply at 53)

In determining whether to launch new programming networks, Fox first determines whether there is an audience for the program network under consideration, then determines the chances of achieving carriage at the levels necessary for commercial success, which is 30-35 million homes to attract national advertising revenues. Both elements – viewership interest and ability to



achieve carriage – are vital to the future success of any programming network. As the above discussion makes clear, the acquisition of DIRECTV will not affect News Corp.'s analysis of whether to launch new programming networks.

9. ***Many local television stations negotiate to receive retransmission compensation from DIRECTV. Will Fox Owned and Operated stations continue to negotiate in the same manner with DIRECTV for retransmission compensation if this deal is completed?***

***If you anticipate any changes in the negotiations between Fox Owned and Operated stations and DIRECTV, how, if at all, do you anticipate those changes will affect the retransmission consent negotiations between DIRECTV and Fox affiliate stations?***

DIRECTV's negotiations with Fox Owned and Operated broadcast television stations for retransmission consent would be considered a "related party transaction" under the Hughes Bylaws and therefore would be subject to review by the independent Audit Committee of the Board. Such negotiations can therefore be expected to continue to be conducted at arm's length and consistent with marketplace conditions, for both Fox owned and affiliated stations.

10. ***News Corp. has proposed to address the concerns that have been raised about this deal, in part, with an independent audit committee of the Hughes Board. What will ensure that the Audit Committee has enough information to act as a check on Hughes' News Corp. appointed management?***
11. ***Many recent corporate scandals demonstrate that even independent audit committees may not work effectively if they are not active and involved. How can News Corp. ensure that Hughes' Audit Committee is active and attentive?***
12. ***What steps will News Corp. take to ensure that it prevents confidential pricing information about DIRECTV's competitors from reaching DIRECTV management?***

A complete response to Questions 10-12 can be found in the Joint Reply and the accompanying Affidavit of Professor Hamermesh, which comprehensively refute unfounded attacks on the efficacy of the corporate governance safeguards that will preclude any anticompetitive foreclosure strategies once News Corp. acquires an interest in Hughes. (Joint Reply at 53-59) As Professor Hamermesh concludes:

The governance arrangements and legal requirements applicable to Hughes in the contemplated transaction are well designed to ensure the participation of directors who will be meaningfully and reliably independent of News Corp. in bargaining effectively and on an arm's length basis with respect to any transaction between News Corp. or any of its affiliates, on one hand, and Hughes or any of its subsidiaries, on the other. (Hamermesh Affidavit, ¶ 12)

The Hughes By Laws give the Audit Committee the express authority to (1) retain counsel and consultants to assist it in carrying out its responsibilities, (2) utilize internal subject matter experts, including DIRECTV, and (3) engage advisors to assist in its review of related party

transactions. The Hughes Directors' fiduciary duty is to all the Hughes shareholders, not just to News Corp. In this era of heightened sensitivity to director responsibilities, Directors with fiduciary obligations to all stockholders and liability under securities laws will avail themselves of expert advice where needed to assist them in evaluating related party transactions.

Contracts between News Corp. and third parties that contain confidential pricing information also typically contain provisions that prohibit disclosure of that information. These provisions are standard, and can and have been sought by cable and satellite competitors to DIRECTV in their programming agreements with News Corp. Disclosure by News Corp. would constitute a breach of its obligations, and cable and satellite competitors could pursue severe remedies, including termination of the contract and injunctive relief. News Corp. does not intend to disclose proprietary or confidential information of any third party to DIRECTV management.

## QUESTIONS OF SENATOR KOHL

1. *Mr. Murdoch, News Corporation has adopted a strategy of significantly outbidding its competitors and paying large amounts to gain exclusive rights to highly demanded sports programming. For example, News Corporation acquired the exclusive rights to show British soccer's Premier League – the equivalent of the NFL in the United States – on the BSkyB satellite service in Britain. In 2001, you paid more than \$1.5 billion to acquire these rights. With respect to sports programming not yet carried on News Corporation broadcast or cable television networks (and thus outside your commitments with respect to the sports programming News Corporation currently carries), can you commit to us that News Corporation will not seek to gain exclusive rights to such programming to be carried by only DIRECTV? If your answer is in any respect other than in the affirmative, do we have any reason to worry that News Corporation will attempt a similar strategy in the United States of gaining exclusive right to sports programming for DIRECTV in order to gain more viewers for DIRECTV and deny essential programming to your competitors?*

News Corp. does not control whether sports programming is offered exclusively to any distributor. That decision is within the power of the various sports leagues and individual teams. If a league or a team decides on its own to offer an exclusive package of games to the marketplace, then DIRECTV should have the ability to compete against cable operators and EchoStar for the right to offer its subscribers that package. Otherwise, DIRECTV would be ceding exclusivity to DISH TV or the dominant cable operator and depriving its own subscribers of the opportunity to receive valued programming. There is no reason why DIRECTV should be singled out in this way and saddled with a more onerous regulatory regime than is the dominant player in the MVPD market – cable.

- 2(a). *The commitments that News Corporation has announced it will abide by after consummation of this transaction include a promise that neither News Corporation nor DIRECTV “will discriminate against unaffiliated programming services with respect to the selection of programming services for carriage or the price, terms or conditions of carriage on the DIRECTV platform.” Please describe what this commitment will mean in practical terms. For example, does this mean that any non-affiliated programming channel or network will be carried on DIRECTV on the same tier and in similar channel placement as the corresponding News Corporation channel or network?*
- 2(b) *We are concerned with the ability of independent programmers not affiliated with any large media conglomerate to obtain carriage on video distribution platforms such as DIRECTV. Will DIRECTV commit to carry independent programming once this transaction is completed? What exactly will that commitment be? Will the commitment be the same with respect to programming that competes with News Corporation programming as to programming that does not?*

News Corp. and DIRECTV have committed not to discriminate against unaffiliated programming services in the selection, price, terms or conditions of carriage. Thus, News Corp.

programming, pursuant to this commitment, could *not* be treated more favorably than unaffiliated programming with respect to whether they are carried on the same tier or have similar channel placement.

This commitment also extends, on its face, to *carriage* of unaffiliated programming networks on DIRECTV. Thus, the analysis for selecting programming for DIRECTV must, under this commitment, be the same for Fox and for unaffiliated programmers.

Aside from the fact that News Corp. and DIRECTV have voluntarily agreed to these nondiscrimination provisions, it should be kept in mind that DIRECTV has only a modest share of the MVPD market (about 13%) and the proposed transaction will not increase that figure. Simply put, DIRECTV does not have a large enough share of the MVPD market to foreclose an unaffiliated programmer, because such programmers would still be able to sell to MVPDs serving 87% of subscribers nationwide. Moreover, such a strategy would only hurt DIRECTV by reducing the attractiveness of its channel lineup. Even when this issue has arisen in the context of an MVPD with much higher market share – as in EchoStar’s proposed acquisition of Hughes where the combined market share would have been 20% – the FCC concluded that the transaction would not create purchasing market power over national or regional programmers. *See EchoStar/Hughes*, 17 FCC Rcd. at 20655.

3. *Last year, when we considered Echostar’s proposal to acquire DIRECTV, one of the asserted benefits was that the combined company would commit to provide local broadcast signals to all 210 markets across the nation. Right now, DIRECTV offers this “local-into-local” service into about 60 markets, but has pledged to expand this service into the 100 largest markets by the end of the year. I believe local-into-local service is essential to make satellite a viable competitor to cable.*

*(a) Mr. Murdoch, News Corporation has committed to “explore the feasibility of aggressively expanding DIRECTV’s local-into-local service.” What does this mean? Can you be more specific with respect to expanding the number of markets to which you will bring local-into-local service, and the dates by which you will reach such targets? Will you agree to make these commitments a condition of approval of your deal?*

*(b) Will News Corporation also agree to offer broadband services to rural communities by specific dates in the future? Please describe how many communities will be covered by this commitment, and by what date.*

As stated in response to Questions 1-4 of Chairman DeWine, News Corp. has a demonstrated commitment to offering local-into-local services, as evidenced by the fact that it was the first to propose such service in connection with its ASkyB venture. News Corp. is a broadcaster, and considers the provision of local-into-local service to as many DMAs as possible to be a vital, priority project. But as the FCC found in the *EchoStar/Hughes* merger proceeding, the pace of technological improvements necessary to make such service feasible in all 210 DMAs is “difficult to predict.” *EchoStar/Hughes*, 17 FCC Rcd. at 20595. Similar uncertainty surrounds

the provision of broadband. Precisely because of this uncertainty, the parties did not attempt to provide any greater details regarding the provision of either local-into-local or broadband service. Moreover, any condition requiring News Corp. to provide such services by a date certain would not be in the public interest, and in fact could threaten the viability of DIRECTV if it proved in the future to be economically or technically infeasible to provide local-into-local or broadband in the manner set forth in such condition.

4. (a) *Mr. Murdoch, while News Corporation's acquisition will make it the largest shareholder in Hughes, owner of DIRECTV, News Corporation will only own 34% of Hughes. In your filing with the FCC, you promise that News Corporation will not purchase a majority interest in DIRECTV for one year after the deal closes. Why did you believe that it was important to make this promise? What problem were you trying to solve?*
- (b) *Why limit this promise to just one year? Why not make this promise effective for a more meaningful period of time, say five years? Would you be willing to make any such commitment promising not to acquire additional shares of Hughes as a condition to approval of this transaction?*

The reason News Corp. committed not to acquire additional shares in Hughes for a period of one year was to comply with Internal Revenue Code requirements to ensure the tax free nature of the split-off of Hughes from General Motors. News Corp. has no current plans to increase its stake in DIRECTV above 34%. However, the analyses set forth in the Joint Reply and economist reports demonstrate that even with a 49% interest in Hughes it would be economically irrational for News Corp. to withhold programming from competing distributors or to raise the cost of its programming above a competitive, marketplace price (Joint Reply at 27 n.66; CRA Report at 50-54). Finally, if and when News Corp. ever decided to acquire 50% or more of Hughes, its interest would shift from *de facto* control to *de jure* control, and FCC approval of the DIRECTV license transfer would again be required.

5. (a) *Mr. Murdoch, News Corporation has promised that any "related party" transaction between News Corp. and DIRECTV must be approved by the audit committee of Hughes Electronics, made up of independent directors. You argue that this should safeguard against "sweetheart deals" between News Corporation and DIRECTV. However, many have criticized this arrangement as ineffective, including Professor Stout of the UCLA Law School. She says in her submission to the FCC that audit committees are not used for this purpose. How can we be satisfied that this audit committee will truly be an independent watchdog to prevent sweetheart deals?*
- (b) *In its filing at the FCC, the Center for Digital Democracy alleges that three of the six people that News Corporation has announced will be the independent directors on the Hughes board – namely, John Thornton, Peter Lund, and Neal Austrian – are not truly independent. The Center for Digital Democracy argues that all three have extensive business relationships with News Corporation. How do you respond*

*to these allegations? What steps are you taking to assure us that the six so-called independent directors will truly be independent of News Corporation?*

- (c) How will the functioning of the Audit Committee change if News Corporation in the future purchases a majority share in Hughes? Specifically, will the Audit Committee continue to function and be constituted entirely by independent directors if News Corporation purchases a majority of Hughes, or if it purchases 100% of Hughes?*
- (d) At the hearing, you stated that it would be impossible for News Corporation to impose supra-competitive programming price increases on DIRECTV because News Corporation will only own a 34% stake in Hughes, and any such price increases would have to be approved by the Hughes Audit Committee. Will the audit committee continue to serve as an independent safeguard on News Corporation's ability to impose programming price increases on DIRECTV if News Corporation obtains a majority stake in Hughes, or if News Corporation purchases 100% of Hughes? If your answer is in the affirmative, explain why.*

Many of these issues are addressed in response to Questions 10-12 of Chairman DeWine, set forth above. The assertions as to the lack of capability and effectiveness of the post-transaction Hughes independent directors flies in the face of the emphasis placed on independent directors in many of the recent corporate governance reforms, such as the Sarbanes Oxley Act, the published rules of the Security and Exchange Commission and the proposed rules of the New York Stock Exchange. Each of the proposed Hughes independent directors will meet all the criteria for "independent" directors established by the SEC and the NYSE. As you are aware, even if News Corp. were to acquire a majority share of Hughes, Sarbanes Oxley, as implemented by the SEC, requires there to be an audit committee of the Board of Hughes comprised entirely of independent directors so long as Hughes is a publicly traded company.

As noted above, the economic incentives against a uniform price increase foreclosure strategy will continue to apply even if News Corp. were to acquire up to 49% of Hughes. Any attempt by News Corp. to acquire a majority share of Hughes will be subject to review and approval by the FCC. At that time, the FCC will have the ability to review the conduct of the parties post-consummation, the effectiveness of corporate governance safeguards, and any other relevant issues to determine whether any additional protections are necessary in the public interest.

6. *(a) Other than the approval of the Hughes Audit Committee, are there any restraints on News Corporation's ability to raise the cost of its programming to DIRECTV?*
- (b) Will News Corporation commit to limit News Corporation's programming price increases in any respect as a condition of approval of this transaction?*
- (c) Will News Corporation agree to limit its programming price increases to no greater than the average rate in increase in cable prices over the past five years? If your answer is in the negative, explain why not.*

The strongest restraint on News Corp.'s ability to raise the cost of its programming to DIRECTV is the fact that DIRECTV and News Corp. lack sufficient market power in any relevant product or geographic market to profitably engage in a so-called "vertical foreclosure strategy." In short, News Corp. does not have the market power to raise the cost of its programming to DIRECTV, and subsequently to DIRECTV's rivals. Cable is still, by far, the dominant competitor, boasting 80% of subscribers compared to DIRECTV's 13%. On the programming side, content vertically integrated with cable constitutes 35% of the most popularly rated prime time cable programming and 45% of the most subscribed-to programming. News Corp.'s share of the programming market is much smaller: fewer than 4% of the national channels and fewer than 10% of the regional channels, which includes only two of the top 20 cable programming services ranked by prime time rating, and none of the top 20 cable programming services ranked by subscribership. As the Joint Reply and the economic analyses attached thereto explain in greater detail, any attempt at "foreclosure" would not enable DIRECTV to achieve the enormous increases in subscribership or pricing that would be necessary to make such a strategy profitable. (Joint Reply at 18-23; CRA Report at 30-50, 55-65; Lexecon Report at 25-27) Thus, it is clear that any pricing condition on News Corp.'s proposed acquisition would have the opposite of the intended effect – *i.e.*, it would benefit cable operators and disadvantage DIRECTV by subjecting only DIRECTV to what would amount to rate regulation. Should the Subcommittee determine that rate regulation is necessary for vertically integrated MVPDs, such regulation should, at a minimum, apply to the dominant MVPDs – cable operators.

7. ***Mr. Murdoch, News Corporation owns over 42 percent of Gemstar, which makes the industry's leading Electronic Programming Guide (EPG) serving over 100 millions viewers nationwide. EPGs are essential to viewers of satellite TV and digital cable, given the hundreds of channels viewers receive. And this dominance in EPGs will continue in the future – Gemstar holds virtually every patent governing use of EPGs. Many are concerned that your ownership of Electronic Programming Guides will enable you give preference to News Corporation programming over your competitor's programming. How can you assure us that this will not occur?***

News Corp.'s interest in Gemstar already exists, and is not altered in any way by the proposed transaction. Thus, if it were really possible for News Corp. to obtain favorable treatment for its programming on the Gemstar EPG, it would be possible regardless of this transaction. The fact that News Corp. has not obtained such favorable treatment suggests strongly that neither News Corp. nor Gemstar has sufficient market power for such a strategy to be economically rational in the first place. In any event, questions related to Gemstar's alleged dominance in the EPG market in no way arise from this transaction, and thus are completely unrelated to consideration of the proposed deal. Rather, as the FCC has appropriately indicated in the past, any such issues should be raised, if at all, in a general, industry-wide proceeding. See AT&T/MediaOne, 15 FCC Rcd. 9816, 9858 (2000).

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SUBMISSIONS FOR THE RECORD

Testimony of Scott Cleland, CEO of the Precursor Group®

Hearing on:

**The NewsCorp/DirecTV Deal: The Marriage of Content and Global Distribution  
Before the U.S. Senate Judiciary Antitrust Subcommittee, June 18<sup>th</sup>, 2003**

Mr. Chairman, thank you for the honor of testifying before your Subcommittee and for the Subcommittee's interest in an independent analyst perspective on the NewsCorp/Hughes proposed merger.

**I am Scott Cleland, a telecom-media investment analyst with expertise in antitrust and mergers.**

- I am also **founder and CEO of the Precursor Group®**, an independent research broker-dealer, which provides investment research to institutional investors covering the technology, telecom and media sectors.
  - Precursor's business interests are aligned with investors' interests – actual and perceived.
  - We do no investment banking for companies; do not manage money or trade for proprietary gain; and our researchers may not trade individual stocks.
- In addition, I am **Chairman of the Investorside Research Association**, an association of 26 independent research providers that work for investors and do not have investment banking conflicts of interest.

**My overall view is that this merger does not anti-competitively harm consumers or competitors.**

While this merger does not raise serious antitrust problems, it does raise significant public policy issues that would best be addressed by the FCC in an industry-wide rulemaking or by Congress in legislation if the FCC or Congress were so inclined. **As an investment analyst, we have advised our clients that we believe this merger will create value for investors.**

My testimony has three parts:

- A. Understanding the Industry Dynamics Underlying This Merger
- B. Why This Merger Is Not an Antitrust Problem, but a Regulatory Issue
- C. Understanding the Regulatory Context



#### A. Understanding the Industry Dynamics Underlying This Merger:

As an independent investment analyst, I view this merger as a logical next step for these companies. It better positions them to compete going forward, while not harming consumers. The combination of NewsCorp's content with DirecTV's DBS distribution platform **solves several critically important and thorny strategic problems for NewsCorp.**

1. **Analog to Digital Migration:** In one fell swoop, NewsCorp becomes a fully digital distributor, legally bypassing the snail-pace, snake-bit, all-cost-little-gain, migration of over-the-air broadcast analog businesses to HDTV.
2. **Regional to National Distribution:** This merger enables NewsCorp to legally bypass the FCC media ownership limit that arbitrarily caps broadcast ownership to 45% of the nation's footprint, and to become a more valuable national distributor of programming.
3. **Advertising to Subscription Model:** The merger enables NewsCorp to transform from a less valuable advertising-dependent model, which is sensitive to economic cycles, to a more valuable subscription-based model, which is not economic cycle sensitive.
4. **Single Channel to Multi-channel:** The merger enables NewsCorp to escape the island of one big broadcast channel to leveraging many channels, which enables more narrowcasting flexibility to meet the clear demand trend for more niche programming.
5. **Un-secure to More Secure Platform:** The merger enables more of Fox's programming to be transmitted over the more secure and controlled DBS distribution platform and less over the over-the-air broadcast platform, which is increasingly vulnerable to piracy from Napster-like file-sharing and to pricing pressure from ad-zapping via TIVO-like technology.
6. **Depreciating to Appreciating Business Model:** This merger enables NewsCorp to switch horses mid-race from the tired-old over-the-air broadcast model, which is near to being put out to pasture, to the new DBS thoroughbred, which is in its prime.
7. **Un-leveraged to Leveraged Distribution:** NewsCorp understands that negotiating leverage increases dramatically with other programmers, if you are also a major distributor.

Mr. Murdoch has had the strategic vision of integrating DBS with content for over six years. I remain very surprised at the lack of similar vision at Disney and Viacom. They remain wedded to yesterday's technology without a workable vision to thrive in a fully digital world. I personally will be surprised if

one of the other big broadcast players does not eventually merge with EchoStar to enjoy the same strategic benefits NewsCorp will gain by merging with DirecTV.

**B. Why This Merger Is Not an Antitrust Problem, but a Regulatory Issue:**

Unlike the EchoStar-DirecTV merger, which Precursor immediately advised investors would not get approved by anti-trust authorities, Precursor's antitrust analysis of this deal has surfaced little antitrust problems that would threaten government approval. We have advised investors that there is a very low level of approval risk with this deal. None of the competitive issues or concerns around this merger raises serious or un-resolvable antitrust problems. There are no significant horizontal concentration issues, and the vertical issues are dramatically less problematic than the much larger Comcast-AT&T Broadband merger, which did not trigger antitrust ire.

Moreover, NewsCorp has a consistent history of being the type of competitor that antitrust authorities actually like – a **maverick competitor** that is unwilling to play the friendly oligopolistic game of not upsetting the status quo. **NewsCorp is the type of aggressive disruptive competitor that generally serves consumer interests well.**

The potential competitive problems this merger could raise are not antitrust issues but more appropriately legislative or regulatory issues. That's because the DBS industry is an artificial government-created and licensed market that needed the landmark program access protections from predatory cable practices in order to become a viable industry. The government initially licensed spectrum for four DBS providers, but the market would only fund and support two: DirecTV and EchoStar.

**C. Understanding the Regulatory Context:**

I would argue that NewsCorp's preemptive proposal to subject itself to the program access regulations, that cable is subjected to, tells us more about the state of the programming market than anything else. What the commitment to program access tells us is that DBS still needs program access protection from cable more than it seeks to gain any leverage over other programmers. In a perfect competitive world, a hard-nosed negotiator like NewsCorp would never negotiate with itself and preemptively make major concessions like agreeing to program access. NewsCorp's tactics tell us a lot about how

important program access is to DBS. Without it, they would be in trouble competitively. It also tells us that DBS remains in a subordinate competitive position to cable, further underscoring that this merger is not an antitrust issue.

As for the discussion about rural broadband service by DBS, Congress needs to appreciate that satellite is a badly inferior architecture for delivering interactive real time broadband/data applications or telephony. Precursor expects satellite broadband to be a minor player in the broadband landscape offering service only where there is no telephone or cable provider interested in seriously serving a particular rural community.

Thank you again Mr. Chairman for the honor and opportunity to testify before your Subcommittee on this important matter.



FOR IMMEDIATE RELEASE:  
JUNE 18, 2003

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**Prepared Statement by U.S. Senator Mike DeWine, Chairman of the Senate Judiciary Subcommittee on Antitrust, Competition Policy, and Consumer Rights, hearing about "The News Corporation/DIRECTV Deal: The Marriage of Content and Global Distribution"**

Good afternoon and welcome to the Antitrust Subcommittee hearing on the proposed transaction between News Corporation and DIRECTV. Just 15 months ago, this Subcommittee held a hearing to examine another deal involving DIRECTV -- the proposed merger between EchoStar and DIRECTV. Many had expressed alarm about this proposed merger and ultimately the Justice Department and the F.C.C. moved to block that deal.

The News Corporation/DIRECTV deal we are examining today is fundamentally different from the merger we examined 15 months ago. Unlike the prior deal, this one does not involve two companies that are direct competitors. Instead, News Corporation and DIRECTV compete in different markets.

In the United States, News Corporation competes primarily as a programmer, owning such properties as the Fox Network and cable networks, such as Fox News Channel and numerous regional sports networks. As a result of this ownership, News Corporation provides some of the most popular programming in the United States.

DIRECTV competes as a distributor of multichannel video programming, providing Direct satellite service to over 11 million subscribers. DIRECTV carries News Corporation programming, and other programming, to subscribers. Thus, this deal is a vertical deal, involving a combination between a supplier of programming, News Corporation, and a distributor of programming, DIRECTV.

Vertical combinations, like this one, can potentially create efficiencies for the combining parties and benefits for consumers.

Vertical deals also, however, can raise competitive concerns, though typically fewer and different kinds of concerns than those raised by deals between direct "horizontal" competitors. Deals such as this one may also raise policy concerns that go beyond antitrust.

In our hearing today, we will explore both the potential efficiencies and benefits of News Corporation's combination with DIRECTV and the concerns that the deal raises.

News Corporation and DIRECTV argue that numerous benefits will flow from their merger. News Corporation will bring its years of experience as a satellite operator in other countries, and its record as an aggressive, innovative competitor to the American video marketplace. For example, in other countries, News Corporation (or News Corp.) has introduced several interactive features, such as interactive shopping and interactive games with its satellite services.

If, in fact, News Corp. is successful in strengthening the competitive offerings of DIRECTV, that would likely force Echostar and the cable systems to improve their product as well, to the benefit of all pay-tv consumers. More specifically, the parties plan to explore aggressively expanding DIRECTV's local-into-local service into more of the 210 local television markets. This is an important potential benefit, and we will examine carefully how the parties plan to expand that service, and we will examine other potential benefits, as well.

Additionally, we must examine the concerns that have been raised about this deal. First and foremost, we must examine concerns that this deal will lead to higher prices for both cable and DBS subscribers. In short, the scenario that critics fear most is one in which News Corp. raises prices to DIRECTV, then wields DIRECTV as a club to batter cable companies into accepting higher prices as well - - all at the expense of consumers.

More generally, critics of this deal have raised concerns about whether News Corp. will use its additional leverage as an anticompetitive weapon to unfairly disadvantage other programmers and distributors. These are complicated issues that need to be examined very carefully.

To their credit, the parties have proposed ways to address some of these concerns. Specifically, News Corp. has promised that it will abide by the program access rules, even under circumstances when those rules technically would not apply to a News Corp./DIRECTV combination. News Corp. also plans to establish an audit committee of the DIRECTV board of directors, which would ensure News Corp. deals fairly with DIRECTV. We will explore whether these protections are sufficient to ease the concerns that have been raised about the deal.

Finally, we also must look beyond the confines of this specific deal to its broader implications for competition in the industry. This Subcommittee has to ask whether the News Corp./DIRECTV transaction will set in motion a series of mergers between large content companies and distributors.

Such consolidation might leave the media in the hands of fewer and fewer vertically integrated companies -- companies with enough market power to effectively exclude independent programmers and raise prices, both to the detriment of American consumers and the marketplace of ideas.

Clearly, this is an important transaction, which, if approved, would have a significant impact on how American consumers receive their news, information, sports, and entertainment. We have a lot to discuss today and I look forward to hearing from our witnesses.

I now turn to the Subcommittee's ranking member, Senator Kohl.

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Testimony of

**EDDY W. HARTENSTEIN**  
Chairman and CEO of DIRECTV, Inc.

before the

**United States Senate Committee on the Judiciary**  
**Subcommittee on Antitrust, Competition Policy and Consumer Rights**

on

**"The News Corp./DIRECTV Deal: The Marriage of Content and Global  
Distribution"**

**June 18, 2003**

**TESTIMONY OF EDDY W. HARTENSTEIN  
Chairman and Chief Executive Officer  
DIRECTV, Inc.  
before the  
U.S. Senate Committee on the Judiciary  
Subcommittee on Antitrust, Competition Policy and  
Consumer Rights  
June 18, 2003**

Chairman DeWine, Senator Kohl, and Members of the Subcommittee, thank you for inviting me to appear before the Subcommittee. I appreciate the opportunity to tell you why the split-off of Hughes Electronics ("Hughes"), the parent company of DIRECTV, Inc., from General Motors Corporation ("GM") and the purchase of a 34% interest in Hughes by News Corp., will benefit consumers throughout the United States, whether they are current or future DIRECTV subscribers, or even cable subscribers. As a direct result of this transaction, DIRECTV will be able to improve its service offerings to U.S. consumers and to provide a stronger competitive alternative to cable operators.

Yesterday was the ninth anniversary of the launch of the DIRECTV® service. Despite the rapid growth of direct broadcast satellite ("DBS") since 1994, cable remains the dominant provider of multi-channel pay television in the United States. Cable operators serve approximately 69 million subscribers and pass an estimated 97.5% of U.S. households.<sup>1</sup> In comparison, DBS operators serve about 20 million subscribers.

Mergers and acquisitions of cable operators, as well as the trading and swapping of systems, have resulted in a significant consolidation and clustering of cable

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<sup>1</sup> Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming, *Ninth Annual Report*, MB Docket No. 02-145, FCC 02-338 at ¶¶ 19 and 29 and Tbls. 1 and 4 (released Dec. 31, 2002) ("*Ninth Annual Report*").



operations. Currently, the ten largest cable operators serve about 85% of all U.S. cable subscribers.<sup>2</sup>

Until 1994, there were no serious competitive alternatives to the dominant cable operators. With the launch of DIRECTV's DBS service, consumers gained access to an alternative provider that offered more channels and superior picture and sound quality as compared to cable. It was not until November 1999, however, when Congress changed the Communications Act and copyright law to allow satellite carriers to retransmit local broadcast channels, that DBS was able to offer a truly competitive alternative to cable -- at least in those markets in which DBS operators are able to provide local broadcast channels.

The benefits to consumers from DBS competition to cable have been tremendous. As the Federal Communications Commission ("FCC") has noted, in markets in which cable has faced competition from DBS operators offering local broadcast channels, cable operators have responded "in a variety of ways, including lowering prices or adding channels without changing the monthly rate, as well as improving customer service and adding new services such as interactive programming."<sup>3</sup> Recently, in a direct response to DBS competition, cable operators have aggressively upgraded their services, including by offering digital cable -- which is perceived by consumers to be qualitatively as good as DBS -- and by combining programming with cable modem services and Internet broadband access packages. Indeed, it is forecast that in the near future -- for the first time -- the number of digital

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<sup>2</sup> *Id.* at ¶ 14.

<sup>3</sup> *Id.* at ¶ 9.

cable subscribers will exceed the total number of DBS subscribers served by DIRECTV and EchoStar combined.<sup>4</sup>

Such developments underscore the need for DBS operators to keep pushing the competitive envelope and to keep innovating, or satellite TV customers will be left behind. DIRECTV already has begun charting this course. For example, in January we announced our intent to offer local channels in more than 100 television markets by the end of this year. Today we offer local channels in 61 markets and are on track to meet our goal of more than 100 markets, assuming the successful launch of our second spot beam satellite in the fourth quarter of this year. We also plan to introduce on July 1 a new high-definition television programming package that will contain four high-definition programming channels, including ESPN HD and Discovery HD Theater, as well as special events broadcast in high-definition.

But we simply cannot stop there. In order to continue improving our service, it is critical that we keep expanding DIRECTV's programming offerings, and keep providing new and innovative services to consumers.

At a time when DIRECTV requires capital to continue to innovate and compete, however, DIRECTV's ultimate parent company, GM, is focused on improving its core automotive operations and addressing the need to provide funding for its U.S. pension plans. While DIRECTV has sufficient funding for its current business plans, should circumstances change or if we choose to pursue new initiatives to remain competitive with cable, DIRECTV may need additional funding. It is unlikely that GM will provide such funding. And seeking additional funding in the form of debt also would be difficult

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<sup>4</sup> See, e.g., Press Release, Leichtman Research Group, "Digital Cable Poised to Overtake DBS (rel. Feb. 25, 2003) (available at [www.leichtmanresearch.com/press/022503release.pdf](http://www.leichtmanresearch.com/press/022503release.pdf)).

because an increase in DIRECTV's debt load would cause downward pressure on GM's credit rating.

GM has recognized that an independent Hughes and DIRECTV will have more flexibility to obtain the financing that DIRECTV needs to grow and remain competitive in the future. In addition, GM recognizes that the support of a company with a core competence in the satellite and media industries would enhance DIRECTV's operations in a variety of ways. After much consideration, GM identified News Corp. as an ideal partner for Hughes and DIRECTV. News Corp. has a proven track record as a global direct-to-home (DTH) service provider and brings a wealth of experience and a history of innovation to Hughes and DIRECTV.

We believe that the proposed split-off of Hughes from GM, and the infusion of investment and entrepreneurial spirit by News Corp., will continue DIRECTV's evolution into a stronger, more capable competitor to cable. As an independent company, and with News Corp. as a significant investment partner, Hughes will take the DIRECTV business to the next level -- increasing and enhancing DIRECTV's service offerings even further, and improving the efficiency and quality of DIRECTV's operations. These results in turn will yield significant benefits to consumers.

For example, with News Corp.'s support, we intend to increase the number of television markets in which DIRECTV provides local broadcast channel service as quickly as is technologically and economically feasible. Individuals residing in those local markets will be able to obtain satellite-delivered news, weather and sports via their local broadcast stations along with the rest of DIRECTV's diverse programming. And

cable operators in these smaller markets will be forced to improve their services in response. For these consumers, it will be a win-win situation.

News Corp. also brings a history of technological innovation and DTH expertise that will be of great value to DIRECTV. Through our combined efforts, we anticipate being able to improve DIRECTV's technology and increase the efficiency of our use of scarce spectrum resources. Based on this greater efficiency, we intend to expand even further the number of HDTV channels that we offer. Our increased carriage of HDTV programming should encourage consumers to invest in HDTV reception equipment, which in turn will drive an even greater demand for HDTV programming.

DIRECTV's commitment to diversity in programming also will be strengthened by its affiliation with News Corp. Historically, News Corp. has produced and supported a wealth of culturally, ethnically, and linguistically diverse programming through its Fox film divisions, television network and broadcast stations. We plan to tap into News Corp.'s resources to expand the diversity of DIRECTV's program offerings.

In sum, the future looks bright for DIRECTV. Independence from GM and the investment by News Corp. will allow DIRECTV to improve and expand its services, and to continue to drive competition in multichannel video programming distribution. As a consequence, consumers will be offered more programming choices and higher quality services -- a result that is manifestly in the public interest.

I realize that I appeared before this Subcommittee just over a year ago touting the benefits of a different transaction. As you know, the Justice Department and the FCC prevented us from consummating that transaction. I believe that the current transaction raises none of the concerns that the DOJ and FCC cited in connection with

the prior transaction. For that reason, I am hopeful that these agencies will allow us to move forward quickly with the News Corp. transaction so that we may continue aggressively to pursue the strategy we have pursued since our launch in 1994 -- to offer the best competitive alternative to cable.

I appreciate the opportunity to share my views.

In connection with the proposed transactions, on June 5, 2003, General Motors Corporation ("GM"), Hughes Electronics Corporation ("Hughes") and The News Corporation Limited ("News") filed preliminary materials with the Securities and Exchange Commission ("SEC"), including a Preliminary Proxy Statement of GM on Schedule 14-A, a Registration Statement of Hughes on Form S-4 and a Registration Statement of News on Form F-4 that contain a consent solicitation statement of GM, a prospectus of News and a prospectus of Hughes. These materials are not yet final and will be amended. Investors and security holders are urged to read the definitive versions of these materials, as well as any other relevant documents filed or that will be filed with the SEC, as they become available, because these documents contain or will contain important information. The preliminary materials filed on June 5, 2003, the definitive versions of these materials, other relevant materials (when they become available), and any other documents filed by GM, Hughes or News with the SEC, may be obtained for free at the SEC's website, [www.sec.gov](http://www.sec.gov), and GM stockholders will receive information at an appropriate time about how to obtain transaction-related documents for free from GM.

GM and its directors and executive officers and Hughes and certain of its executive officers may be deemed to be participants in the solicitation of proxies or consents from the holders of GM \$1-2/3 common stock and GM Class H common stock in connection with the proposed transactions. Information about the directors and executive officers of GM and their ownership of GM stock is set forth in the proxy statement for GM's 2003 annual meeting of shareholders. Participants in GM's solicitation may also be deemed to include those persons whose interests in GM or Hughes are not described in the proxy statement for GM's 2003 annual meeting. Information regarding these persons and their interests in GM and/or Hughes was filed pursuant to Rule 425 with the SEC by each of GM and Hughes on April 10, 2003. Investors may obtain additional information regarding the interests of such participants by reading the preliminary consent solicitation statement of GM / prospectus of Hughes / prospectus of News filed with the SEC on June 5, 2003 and the definitive consent solicitation statement of GM / prospectus of Hughes / prospectus of News when it becomes available.

This communication shall not constitute an offer to sell or the solicitation of an offer to buy any securities, nor shall there be any sale of securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction. No offering of securities shall be made except by means of a prospectus meeting the requirements of Section 10 of the Securities Act of 1933, as amended.

Materials included in this document contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that could cause actual results to be materially different from historical results or from any future results expressed or implied by such forward-looking statements. The factors that could cause actual results of GM, Hughes and/or News to differ materially, many of which are beyond the control of GM, Hughes or News include, but are not limited to, the following: (1) operating costs, customer loss and business disruption, including, without limitation, difficulties in maintaining relationships with employees, customers, clients or suppliers, which may be greater than expected following the transaction; (2) the regulatory approvals required for the transaction may not be obtained on the terms expected or on the anticipated schedule; (3) the effects of legislative and regulatory changes; (4) an inability to retain necessary authorizations from the FCC; (5) an increase in competition from cable as a result of digital cable or otherwise, direct broadcast satellite, other satellite system operators, and other providers of subscription television services; (6) the introduction of new technologies and competitors into the subscription television business; (7) changes in labor, programming, equipment and capital costs; (8) future acquisitions, strategic partnerships and divestitures and

the ability to access capital to maintain financial flexibility; (9) general business and economic conditions; and (10) other risks described from time to time in periodic reports filed by GM, Hughes or News with the SEC. Those other risks relating to Hughes include, but are not limited to, the uncertainties regarding the operations of DIRECTV Latin America, LLC, Hughes' 75% owned subsidiary, which is currently operating under Chapter 11 bankruptcy proceedings, and the performance of its satellites. You are urged to consider statements that include the words "may," "will," "would," "could," "should," "believes," "estimates," "projects," "potential," "expects," "plans," "anticipates," "intends," "continues," "forecast," "designed," "goal," "outlook," "objectives," "strategy," "target," or the negative of those words or other comparable words to be uncertain and forward-looking. This cautionary statement applies to all forward-looking statements included in this document.



News Release  
**JUDICIARY COMMITTEE**

*United States Senate • Senator Orrin Hatch, Chairman*

June 18, 2003

Contact: Margarita Tapia, 202/224-5225

**Statement of Chairman Orrin G. Hatch  
Before the United States Senate Committee on the Judiciary  
Subcommittee on Antitrust, Competition, and Business and Consumer Rights  
Hearing on**

**“THE NEWSCORP/DIRECT TV DEAL:  
THE MARRIAGE OF CONTENT AND GLOBAL DISTRIBUTION”**

I want to start by thanking the Chairman of the Antitrust Subcommittee, Senator DeWine, and the Ranking Democratic Member, Senator Kohl, for holding this important hearing to examine the NewsCorp/Direct TV transaction.

NewsCorp’s acquisition of a controlling interest in Direct TV raises important public policy issues relating to competition and diversity of viewpoints in our country’s media market place. The Judiciary Committee as a whole, and the Antitrust Subcommittee in particular, must continue to examine the critical issues surrounding increased concentration of our Nation’s media outlets as they arise in regulatory and enforcement contexts. The NewsCorp acquisition – like so many of the recent media acquisitions – requires us to weigh the benefits of such a transaction against the potential for reduced competition in media markets.

There has been much controversy surrounding media ownership, given the Federal Communications Commission’s recent decision to relax its media ownership regulatory requirements, and the Justice Department’s approval of several media acquisitions. These issues are complex and require careful consideration of specific market place factors and the potential for competitive harm. When it comes to ensuring competition and diversity in our media markets, I have not -- and will not -- analyze the issue by blindly condemning all merger consolidations. To me, “big” is not necessarily bad. Rather, the issue of media consolidation requires a careful weighing of our Nation’s interest in promoting competition and diversity.

In my view, such an analysis requires examination of the potential for anti-competitive conduct, rather than adherence to inflexible regulatory restrictions or hard and fast enforcement rules. Market forces – not federal across-the-board regulations – will ensure that consumers benefit from a transaction. To this end, traditional antitrust enforcement will



more effectively and efficiently protect competition and enhance diversity than regulatory one-size-fits-all approaches.

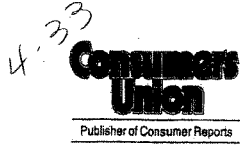
With these principles in mind, I want to turn to the specific NewsCorp acquisition. Overall, it is important to remember that the competitive implications of the NewsCorp acquisition of a controlling interest in Direct TV are far different than those raised two years ago by the proposed merger between EchoStar and Direct TV, which was eventually blocked by the Justice Department and the Federal Communications Commission. Unlike the EchoStar-DirectTV, the NewsCorp transaction does not raise traditional "horizontal" merger concerns which result in reduced competition among existing competitors; however, the NewsCorp acquisition requires analysis of the "vertical" implications of the marriage of NewsCorp, a significant content supplier, and Direct TV, a multi-channel video distributor.

NewsCorp does not own any United States-based satellite distribution facilities, but does own programming assets, including 20<sup>th</sup> Century Fox, the Fox Network, and the FoxNews Channel. Direct TV and EchoStar control over 90 percent of the United States Direct Broadcast Satellite market, but only about 20 percent of the broader multi-channel video distribution market, which continues to be dominated by cable television systems serving approximately 75 percent of the national multi-channel video market.

The combination of NewsCorp and Direct TV may result in significant benefits to viewers across the country by injecting additional competition in the multi-channel video market. NewsCorp has been an innovative competitive force in the United States and globally. With this acquisition, NewsCorp may be in an even better position to compete with cable television and EchoStar, Direct TV's primary DBS competitor, and deliver new and innovative programming services. At the same time, we need to examine whether or not there is any real potential for anti-competitive behavior by NewsCorp or Direct TV that may outweigh the overall benefits this merger could provide.

I look forward to hearing from Mr. Murdoch and other witnesses today concerning this important transaction and the impact it will have on markets across the country.

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**Testimony of Gene Kimmelman,  
Senior Director for Advocacy and Public Policy,  
Consumers Union**

**Before the  
Antitrust, Competition Policy and Consumer Rights Subcommittee  
of the  
Senate Judiciary Committee**

**On  
News Corp./DirecTV Merger**

June 18, 2003

## SUMMARY

Consumers Union<sup>1</sup> welcomes this opportunity to testify before the Senate Antitrust, Competition Policy and Consumer Rights Subcommittee regarding the proposed merger between the News Corporation ("News Corp.") and Hughes Electronics Corporation's satellite television unit DIRECTV ("DirecTV"). Given the current concentration in the media marketplace, as well as the further concentration that will result from the Federal Communications Commission's (FCC's) recent relaxation of media ownership rules, we believe that the proposed merger between network and cable giant News Corp. and DirecTV, the largest direct broadcast satellite (DBS) service provider, will further increase prices for consumers and decrease the diversity of voices in the media marketplace.

Today, consumers are not receiving the fruits that a competitive cable and satellite marketplace should deliver, and consumers are likely to suffer further harm if antitrust officials do not impose substantial conditions on the proposed deal between News Corp. and DirecTV. Since passage of the 1996 Telecommunications Act, cable rates have risen over 50%,<sup>2</sup> and FCC data show that satellite competition is not creating downward pressure on cable rates. Despite the promise for more diversity from new technologies such as the Internet and satellite, a mere five media companies control nearly the same prime time audience shares as the Big Three networks did 40 years ago.<sup>3</sup> Unfortunately, the market for news production and distribution is becoming more concentrated.

And a troubling situation is about to get much worse.

The recently announced proposed merger between News Corp. and DirecTV, combined with the FCC's decision two weeks ago to significantly weaken its media ownership regulations, threaten to seriously harm meaningful competition between media companies in this nation. This lack of competition will mean that control of the media that Americans rely upon most for news, information and entertainment will likely be placed in the hands of a few powerful media giants.

The FCC's June 2<sup>nd</sup> order dramatically reworked the rules that protected the diversity, localism, and competition of the media in this country. Under the new rules, mergers between television stations and newspapers in a single community will now be allowed in approximately 200 markets comprising 98 percent of the population. Ownership of two or even three television stations by one company are allowed in over 160 U.S. markets under the new FCC rules. In these markets, the new rules do not provide for any public interest review of such mergers. The

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<sup>1</sup> Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the state of New York to provide consumers with information, education and counsel about good, services, health and personal finance, and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life for consumers. Consumers Union's income is solely derived from the sale of *Consumer Reports*, its other publications and from noncommercial contributions, grants and fees. In addition to reports on Consumers Union's own product testing, *Consumer Reports* with more than 4 million paid circulation, regularly, carries articles on health, product safety, marketplace economics and legislative, judicial and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

<sup>2</sup> Bureau of Labor Statistics, Consumer Price Index (March 2003). From 1996 until March 2003, CPI increased 19.3% while cable prices rose 50.3%, 2.6 times faster than inflation.

<sup>3</sup> Tom Wolzien, "Returning Oligopoly of Media Content Threatens Cable's Power." The Long View, Bernstein Research (Feb. 7, 2003).

FCC made these radical rule changes despite the presence of considerable media concentration in eighty to ninety percent of the markets affected by this decision.

The result, according to industry analysts, is that broadcast television station owners will either purchase television stations in new markets, or will swap properties with other large media owners, concentrating ownership of both television station and newspapers within one market in an attempt to achieve cost "synergies." But experience with the television duopolies permitted by waiver prior to the FCC's decision to weaken its rules shows that these "synergies" have come from the elimination of news programming and news reporters and the substitution of a single, centralized news operation in place of multiple, independent news divisions.

The proposed merger of News Corp. and DirecTV comes in the wake of this FCC decision. While the antitrust laws can and should be used to limit potential competitive abuses resulting from the News Corp./DirecTV merger, these laws are not enough to prevent the excessive consolidation in the marketplace of ideas that will result from any combination of transactions under these relaxed ownership rules. Antitrust has never been used effectively to promote competition in and across media where there is no clear way – like advertising prices – of measuring competition/diversity in news sources, information and points of view presented through the media.

Media moguls themselves admit their desire to avoid real competition within their industry. At the National Cable and Telecommunications Conference last week, Mel Karmazin, president and chief operating officer of Viacom, declared in reference to colleagues from Microsoft, AOL Time Warner, and Comcast, "I can't imagine being a competitor with any of these guys."<sup>4</sup>

Consumers Union believes the Department of Justice should impose significant conditions on the News Corp./DirecTV deal, and Congress should alter the laws that enable industry consolidation spurred by excessive deregulation to weaken or undermine competitive conditions in media markets. The News Corp./DirecTV merger is likely to lead to higher prices for both satellite and cable television, since the combined company can maximize its earnings by inflating the prices it charges for its broad array of popular programming that all cable and satellite customers purchase.

We are pleased to see that the combined News Corp./DirecTV entity has agreed to offer access to their programming as part of the acquisition.<sup>5</sup> However, this promise must be expanded to prevent other forms of anticompetitive discrimination, and must be enforceable through appropriate Department of Justice oversight mechanisms.

<sup>4</sup> Richard Linnett, "Media Rivals Backlap at Cable Conference." *AdAge.com*, June 10, 2003.

<sup>5</sup> "As part of the acquisition, News Corp. and DIRECTV has agreed to abide by FCC program access regulations, for as long as those regulations are in place and for as long as News Corp. and Fox hold an interest in DIRECTV. . . Specifically, News Corp. will continue to make all of its national and regional programming available to all multi-channel distributors on a non-exclusive basis and on non-discriminatory prices, terms and conditions. Neither News Corp. nor DIRECTV will discriminate against unaffiliated programming services with respect to the price, terms or conditions of carriage on the DIRECTV platform." News Corporation Press Release, "News Corp. Agrees to Acquire 34% of Hughes Electronics for \$6.6 Billion in Cash and Stock." Apr. 9, 2003.

Even given the terms of what News Corp. is willing to concede by way of program access, substantial danger remains. First, there is a danger that News Corp. will discriminate against non-affiliated programmers in determining what programming to offer on its DirecTV satellite system. News Corp. could also pressure cable operators to do the same in return for more favorable carriage terms for News Corp. owned programming.

Second, the agreement preserves the right to a variety of exclusive carriage arrangements, including distribution of Liberty Media programming, as well as sports programming where News Corp. enjoys substantial market power. Liberty Media owns approximately 18% of News Corp., and News Corp. has interests in several Liberty properties, indicating a close relationship between the two. It is hard to understand how such exclusive arrangements involving a company with such massive market power would not have a detrimental impact on competition in video programming. Antitrust officials must prevent these types of behavior.

We believe it is time for Congress to intervene and finally deliver more choices and lower prices for the media services consumers want, and to reverse the excessive relaxation of media ownership which threatens the critical watchdog function media companies play in our nation's democracy. It is time for Congress to look beyond the rhetoric and focus on the reality of deregulated video markets. Congress should:

- Reconsider its grant of retransmission rights to broadcasters, where a broadcaster also owns a second means of video distribution.
- Let consumers pick the TV channels they want for a fair price.
- Prevent all forms of discrimination by those who control digital TV distribution systems and those who control the most popular programming in a manner that prevents competition in the video marketplace.
- Most importantly, reverse the FCC's decision to weaken media ownership rules that prevented companies from owning the most popular sources of news and information in both the local and the national markets.

### THE NEWS CORPORATION/DIRECTV MERGER

If competition in the multichannel video market had performed up to its hope and hype, the NewsCorp./DirecTV merger might not be so threatening. But in light of the failure of deregulation, it presents a problem for public policy that cannot be ignored. There are two points of power in the marketplace – distribution and program production. The problem with a merger between News Corp. and DirecTV is that it combines the two.

The reach of News Corp.'s media empire is truly staggering. The following are highlights of some News Corp. properties in the U.S.:

- Broadcast Television Stations (35 stations, including two broadcast stations in New York, Los Angeles, Dallas, Houston, Minneapolis, Phoenix and Orlando)
- Filmed Entertainment (20<sup>th</sup> Century Fox Film Corp., Fox 2000 Pictures, Fox Searchlight Pictures, Fox Music, 20<sup>th</sup> Century Fox Home Entertainment, Fox Interactive, 20<sup>th</sup> Century Fox Television, Fox Television Studios, 20<sup>th</sup> Television, Regency Television and Blue Sky Studios)
- Cable Network Programming (Fox News Channel—the most watched cable news channel, Fox Kids Channel, FX, Fox Movie Channel, Fox Sports Networks, Fox Regional Sports Networks, Fox Sports World, Speed Channel, Golf Channel, Fox Pan American Sports, National Geographic Channel, and the Heath Network)
- Publishing (New York Post, the Weekly Standard, HarperCollins Publishers, Regan Books, Amistad Press, William Morrow & Co., Avon Books, and Gemstar – TV Guide International)
- Sports Teams and Stadiums (Los Angeles Dodgers, and partial ownership in the New York Knicks, New York Rangers, LA Kings, LA Lakers, Dodger Stadium, Staples Center, and Madison Square Garden)

News Corp.'s merger with DirecTV adds a new, nationwide television distribution system to News Corp.'s programming/production arsenal. DirecTV is the nation's largest satellite television distribution system, with more than 11 million customers and the ability to serve all communities in the United States.

News Corp.'s vast holdings provide it with leverage in several ways. "The biggest, most powerful weapon News Corp. has is 'a four-way leverage against cable operators, competing with satellite and using the requirement that cable get retransmission consent to carry Fox-owned TV stations, while potentially leveraging price for Fox-owned regional sports networks and its national cable and broadcast networks. . .'"<sup>6</sup>

<sup>6</sup> Diane Mermigas, "News Corp.'s DirecTV Monolith." Mermigas on Media Newsletter, (Apr. 16, 2003), quoting Tom Wolzien, a Sanford Bernstein Media Analyst.

One of News Corp.'s most important weapons is significant control over regional and national sports programming. Mr. Murdoch often describes sports programming as his "battering ram"<sup>7</sup> to attack pay television markets around the world. As David D. Kirkpatrick noted in an April 14, 2003 *New York Times* article regarding Mr. Murdoch's control over sports programming:

In the United States, News Corp.'s Entertainment subsidiary now also controls the national broadcast rights to Major League Baseball, half the Nascar racing season and every third Super Bowl. On cable, Fox controls the regional rights to 67 of 80 teams in the basketball, hockey and baseball leagues as well as several major packages of college basketball and football games, which it broadcasts on more than 20 Fox regional sports cable networks around the country. By acquiring DirecTV, Mr. Murdoch gains the exclusive right to broadcast the entire slate of Sunday NFL games as well.

With DirecTV, Mr. Murdoch can start a new channel with immediate access to its subscribers, currently 11 million. He has other leverage in Fox News, now the most popular cable news channel, and essential local stations in most major markets around the country.<sup>8</sup>

It is important to consider the ramifications of Mr. Murdoch's control of over 40% of Fox broadcast stations nationwide, control of 11.2 million satellite subscribers, and his stranglehold over regional sports programming. With those extensive holdings, News Corp. is in a position to determine what new programming comes to market, and to undercut competitive programming. The company will be able to decide what programming it does not want to carry and may be able to indirectly pressure cable operators (by offering a lower price for Fox programming as an inducement) not to carry programming that competes with Fox offerings. We believe Mr. Murdoch has a right as an owner to put whatever he wants on his system, but with the FCC having voted to weaken the media ownership rules, companies like News Corp. will have the ability to control key sources of news and information in an unprecedented manner.

The merger between News Corp. and DirecTV is extremely unlikely to stop skyrocketing cable rates and could very well exacerbate the problem. According to David Kirkpatrick's *New York Times* article,<sup>9</sup>

some analysts said the structure of the deal suggested Mr. Murdoch hoped to use DirecTV mainly to punish other pay television companies and benefit his programming businesses. The Fox Entertainment Group, an 80 percent-owned subsidiary of News Corporation, will own a 34 percent stake in DirecTV's parent, creating the potential for programming deals that favor Fox over DirecTV.

'My sense is that the major purpose for News Corporation controlling DirecTV is to use it as a tactical weapon against the cable companies to get them to pay up

<sup>7</sup> David D. Kirkpatrick, "Murdoch's First Step: Make Sports Fans Pay." *The New York Times*, Apr. 14, 2003.

<sup>8</sup> *Id.*, Emphasis added.

<sup>9</sup> David Kirkpatrick, "By Acquiring DirecTV, Murdoch Gets Upper Hand." *The New York Times*, Apr. 10, 2003.

for its proprietary programming,' said Robert Kaimowitz, chief executive of the investment fund Bull Path Capital Management.

While News Corp. has agreed to abide by the FCC's program access requirements, this pledge could end up being nothing more than a tool for pumping up cable prices. That is, while News Corp. agrees to make its programming available on non-discriminatory terms and conditions, there is absolutely nothing that would prevent News Corp. from raising the price that it charges itself on its satellite system, in return for increased revenues from the other 70 million cable households. If a cable system refuses to pay the increased price, then News Corp. will be able to threaten cable operators with use of its newly acquired satellite system to capture market share away from cable in those communities.

An article in the *Washington Post*<sup>10</sup> recently detailed the way this might work:

For instance, News Corp. raised the cost of his Fox Sports content to some cable systems by more than 30 percent this year, according to one cable operator. Like most officials interviewed yesterday, he refused to be identified, saying he had to continue dealing with News Corp.

Most recently, in Florida, News Corp. pulled its Fox Sports regional sports programming off of competitor Time Warner Cable's system over a rate dispute. News Corp. wanted to charge more than Time Warner was willing to pay, but the conflict was resolved and service restored. "If this happens when Rupert owns DirecTV, you can assume DirecTV will go into the market and just pound away at the cable system," said one cable channel executive.

And price is only the beginning of the problems in this industry. Even in the 500-channel cable universe, control of prime time programming rests in the hands of a very few media companies. Given the enormous power that will be concentrated in News Corp. as a result of the DirecTV transaction, not only will the combined entity be able to insist on top dollar for its programming, it will be able to determine who makes it and who fails in the programming marketplace.

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<sup>10</sup> Frank Ahrens, *Murdoch's DirecTV Deal Scares Rivals.* *Washington Post*, Apr. 11, 2003.



**CABLE RATES HAVE ESCALATED AND SATELLITE COMPETITION HAS NOT KEPT THEM UNDER CONTROL**

Despite the growth of satellite TV, the promise of meaningful competition to cable TV monopolies remains unfulfilled. Cable rates are up 50% since Congress passed the 1996 Telecommunications Act, nearly three times as fast as inflation.<sup>11</sup> We welcome the possibility that satellite would aggressively cut its price and compete with cable, thereby keeping cable rates in check, but for several reasons that is unlikely to happen.

Satellite competition has failed to prevent price increases on cable because cable and satellite occupy somewhat different product spaces. First and foremost, the lack of local channels on satellite systems in many communities prevents satellite from being a substitute for cable; in fact, many satellite subscribers also purchase cable service for the express purpose of receiving local channels. And while many larger communities now receive local broadcast channels from satellite, service is not as attractive as cable in several respects and many consumers simply cannot subscribe. Many urban consumers cannot receive satellite services because of line of sight problems, or because they live in a multi-tenant dwelling unit where only one side of the building faces south.

Restrictions on multiple TV set hookups also make satellite more costly. The most recent data on the average price for monthly satellite service indicates that consumers pay between \$44 and \$80 a month to receive programming comparable to basic cable programming. This monthly fee often includes two separate charges above the monthly fee for basic satellite programming – one fee to hook a receiver up to more than one television in the household, and another fee so consumers are able to receive their local broadcast channels.

Satellite customers often subscribe to receive high-end services not provided (until the recent advent of digital cable) on cable systems, such as high-end sports packages, out of region programming, and foreign language channels. In essence, it is an expensive – but valuable – product for consumers who want to receive hundreds of channels.

If satellite were a close substitute for cable, one would expect that it would have a large effect on cable. In fact, the FCC's own findings and data have contradicted the cable industry claims for years. The FCC found that satellite only "exerts a small (shown by the small magnitude of DBS coefficient) but statistically significant influence on the demand for cable service."<sup>12</sup> In the same econometric estimation, the FCC concluded that the "the demand for cable service is somewhat price elastic (i.e. has a price elasticity of minus 1.45) and suggests that there are substitutes for cable."<sup>13</sup> This elasticity is not very large and the FCC recognizes that in using the modifier "somewhat." The FCC also attempted to estimate a price effect between satellite and cable. If cable and satellite were close substitutes providing stiff competition, one would also expect to see a price effect. Most discussions of substitutes and price elasticity in

<sup>11</sup> Bureau of Labor Statistics, Consumer Price Index (March 2003). From 1996 until March 2003, CPI increased 19.3% while cable prices rose 50.3%, 2.6 times faster than inflation.

<sup>12</sup> Report on Cable Industry Prices, February 14, 2002, p. 36.

<sup>13</sup> Report on Cable Industry Prices, February 14, 2001, p. 36.

economics texts state that substitutes exhibit a positive cross elasticity.<sup>14</sup> The FCC can find none. In fact, it found quite the opposite. The higher the penetration of satellite, the higher the price of cable.<sup>15</sup>

The most recent annual report on cable prices shows that the presence of DBS has no statistically significant or substantial effect on cable prices, penetration or quality.<sup>16</sup> This is true when measured as the level of penetration of satellite across all cable systems, or when isolating only areas where satellite has achieved a relatively high penetration.<sup>17</sup> At the same time, ownership of multiple systems by a single entity, large size and clustering of cable systems results in higher prices.<sup>18</sup> Vertical integration with programming results in fewer channels being offered (which restricts competition for affiliated programs).<sup>19</sup>

In other words, one could not imagine a more negative finding for intermodal competition or industry competition from the FCC's own data. All of the concerns expressed about concentrated, vertically integrated distribution networks are observed and the presence of intermodal competition has little or no power to correct these problems. The claims that the cable industry makes about the benefits of clustering and large size – measured as price effects – are contradicted by the data. In fact, only intramodal, head-to-head competition appears to have the expected effects. The presence of wireline cable competitors lowers price and increases the quality of service.

While we hope that satellite will ultimately have a price disciplining effect in those communities where satellite offers local broadcast stations it is clear that the single most important variable in cable prices is whether there is a cable overbuilder in a particular

<sup>14</sup> Pearce, George, *The Dictionary of Modern Economics* (MIT Press, Cambridge, 1984), p. 94. Cross Elasticity of Demand. The responsiveness of quantity demanded of one good to a change in the price of another good. Where goods i and j are substitutes the cross elasticity will be positive-i.e. a fall in the price of good j will result in a fall in the demand for good i as j is substituted for i. If the goods are complements the cross elasticity will be negative. Where i and j are not related, the cross elasticity will be zero. Taylor, John, B., *Economics* (Houghton Mifflin, Boston, 1998), p. 59.

A sharp decrease in the price of motor scooters or rollerblades will decrease the demand for bicycles. Why? Because buying these related goods becomes relatively more attractive than buying bicycles. Motor scooters or rollerblades are examples of substitutes for bicycles. A substitute is a good that provides some of the same uses or enjoyment as another good. Butter and margarine are substitutes. In general, the demand for a good will increase if the price of a substitute for the good rises, and the demand for a good will decrease if the price of a substitute falls.

Bannock, Graham, R.E. Bannock and Evan Davis, *Dictionary of Economics* (Penguin, London, 1987).

Substitutes. Products that at least partly satisfy the same needs of consumers. Products are defined as substitutes in terms of cross-price effects between them. If, when the price of records goes up, sales of compact discs rise, compact discs are said to be a substitute for records, because consumers can to some extent satisfy the need served by records with compact discs. This account is complicated by the fact that, when the price of an item changes, it affects both the REAL INCOME of consumers and the relative prices of different commodities. Strictly, one product is a substitute for another if it enjoys increased demand when the other's price rises and the consumer's income is raised just enough to compensate for the drop in living standards caused (pp. 390-391).

Cross-price elasticity of demand. The proportionate change in the quantity demanded of one good divided by the proportionate change in the price of another good. If the two goods are SUBSTITUTES (e.g. butter and margarine), this ELASTICITY is positive. For instance, if the price of margarine increases, the demand for butter will increase (p. 99).

<sup>15</sup> Report on Cable Prices, p. 11.

<sup>16</sup> Federal Communications Commission, 2002b.

<sup>17</sup> Federal Communications Commission, 2001b, describes the DBS variable as the level of subscription. Federal Communications Commission, 2002b, uses the DBS dummy variable.

<sup>18</sup> The cluster variable was included in the Federal Communications Commission 2000a and 2001b Price reports. Its behavior contradicted the FCC theory. It has been dropped from the 2002 report. The MSO size was included in the 2002 report. System size has been included in all three reports.

<sup>19</sup> Vertical integration was included in Federal Communications Commission, 2002b.

community. Wire-to-wire competition does hold down cable rates, whereas satellite seems not to. The U.S. General Accounting office describes this phenomenon:

Our model results do not indicate that the provision of local broadcast channels by DBS companies is associated with lower cable prices. In contrast, the presence of a second cable franchise (known as an overbuilder) does appear to constrain cable prices. In franchise areas with a second cable provider, cable prices are approximately 17 percent lower than in comparable areas without a second cable provider.<sup>20</sup>

In other words, where there are two satellite and one cable company in a market, prices are 17 percent higher than where there are two cable companies and two satellite providers in a market. If we had this type of competition nationwide, consumers could save more than \$5 billion a year on their cable bills.

#### PROGRAM PRODUCTION

The failure of competition in the cable and satellite distribution market is matched by the failure of competition in the TV production market. In the 1980s, as channel capacity grew, there was enormous expansion and development of new content from numerous studios. Policymakers attributed the lack of concentration in the production industry to market forces and pushed for the elimination of the Financial Interest in Syndication rules (Fin-Syn) that limited network ownership and syndication rights over programming. The policymakers were wrong.

Following the elimination of the Fin-Syn rules in the early 1990s, the major networks have consolidated their hold over popular programming. The market no longer looks as promisingly competitive or diverse as it once did. Tom Wolzien, Senior Media Analyst for Bernstein Research, paints the picture vividly—he details the return of the “old programming oligopoly”:

Last season ABC, CBS and NBC split about 23% [of television ratings]. . . But if the viewing of all properties owned by the parent companies – Disney, NBC, and Viacom – is totaled, those companies now directly control television sets in over a third of the TV households. Add AOL, Fox and networks likely to see consolidation over the next few years (Discovery, A&E, EW Scripps, etc.), and five companies or fewer would control roughly the same percentage of TV

<sup>20</sup> U.S. General Accounting Office, *Report to the Subcommittee on Antitrust, Competition, and Business and Consumer Rights, Committee on the Judiciary, U.S. Senate: Issues in Providing Cable and Satellite Television Services.* October 2002. In an important clarifying footnote, the report finds that:

“This was a larger effect than that found by FCC in its 2002 *Report on Cable Industry Prices* (FCC 02-107). Using an econometric model, FCC found that cable prices were about 7 percent lower in franchise areas when there was an overbuilder. One possible explanation for the difference in results is that we conducted further analysis of the competitive status of franchises that were reported by FCC to have an overbuilder. We found several instances where overbuilding may not have existed although FCC reported the presence of an overbuilder, and we found a few cases where overbuilders appeared to exist although FCC had not reported them. We adjusted our measurement of overbuilder status accordingly.”

households in prime time as the three net[work]s did 40 years ago. The programming oligopoly appears to be in a process of rebirth.<sup>21</sup>

In addition, the number of independent studios in existence has dwindled dramatically since the mid-1980s. In 1985, there were 25 independent television production studios; there was little drop-off in that number between 1985 and 1992. In 2002, however, only 5 independent television studios remained. In addition, in the ten-year period between 1992 and 2002, the number of prime time television hours per week produced by network studios increased over 200%, whereas the number of prime time television hours per week produced by independent studios decreased 63%.<sup>22</sup>

Diversity of production sources has “eroded to the point of near extinction. In 1992, only 15 percent of new series were produced for a network by a company it controlled. Last year, the percentage of shows produced by controlled companies more than quintupled to 77 percent. In 1992, 16 new series were produced independently of conglomerate control, last year there was one.”<sup>23</sup>

The ease with which broadcasters blew away the independent programmers should sound a strong cautionary alarm for Congress. The alarm can only become louder when we look at the development of programming in the cable market. One simple message comes through: those with rights to distribution systems win.

Of the 26 top cable channels in subscribers' and prime time ratings, all but one of them (the Weather Channel) has ownership interest of either a cable MSO or a broadcast network. In other words, it appears that you must either own a wire or have transmission rights to be in the top tier of cable networks. Four entities – News Corp. (including cross ownership interests in and from Liberty) AOL Time Warner, ABC/Disney and CBS/Viacom – account for 20 of these 26 channels.

Of the 39 new cable networks created since 1992, only 6 do not involve ownership by a cable operator or a national TV broadcaster. Sixteen of these networks have ownership by the top four programmers. Eight involve other MSOs and 10 involve other TV broadcasters. Similarly, a recent cable analysis identified eleven networks that have achieved substantial success since the passage of the 1992 Act. Every one of these is affiliated with an entity that has guaranteed carriage on cable systems.<sup>24</sup>

Moreover, each of the dominant programmers has guaranteed access to carriage on cable systems – either by ownership of the wires (cable operators) or by carriage rights conferred by Congress (broadcasters).

<sup>21</sup> Tom Wolzien, “*Returning Oligopoly of Media Content Threatens Cable’s Power.*” The Long View, Bernstein Research (Feb. 7, 2003). Emphasis added.

<sup>22</sup> Coalition for Program Diversity, Jan. 28, 2003.

<sup>23</sup> Victoria Riskin, President of Writers Guild of America, West. *Remarks at FCC EnBanc Hearing, Richmond, VA* (Feb. 27, 2003).

<sup>24</sup> Federal Communications Commission, *Ninth Annual Report, In the Matter of Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, MB docket No. 02-145 (Dec. 31, 2002).

- AOL Time Warner has ownership in cable systems reaching over 12 million subscribers and cable networks with over 550 million subscribers.
- Liberty Media owns some cable systems and has rights on Comcast systems and owns cable networks with approximately 880 million subscribers. Liberty owns almost 20% of News Corp.
- Disney/ABC has must carry-retransmission rights and ownership in cable networks reaching almost 700 million subscribers.
- Viacom/CBS has must carry-retransmission rights and ownership in cable networks reaching approximately 625 million subscribers.
- Fox has must carry-retransmission and ownership in cable networks reaching approximately 370 million subscribers and a substantial cross ownership interest with Liberty.

These five entities account for over 60 percent of subscribers to cable networks, rendering this market a tight oligopoly. Other entities with ownership or carriage rights account for four of the five remaining most popular cable networks. The only network in the top 25 without such a connection is the Weather Channel. It certainly provides a great public service, but is hardly a hotbed for development of original programming or civic discourse. Entities with guaranteed access to distribution over cable account for 80 percent of the top networks and about 80 percent of all subscribers' viewing choices on cable systems.

In the world of broadcast and cable networks, almost three-quarters of them are owned by six corporate entities.<sup>25</sup> The four major TV networks, NBC, CBS, ABC, Fox, and the two dominant cable providers, AOL Time Warner (which also owns a broadcast network) and Liberty (with an ownership and carriage relationship with Comcast and Fox), completely dominate the tuner. Moreover, these entities are thoroughly interconnected through joint ventures.

If distribution rights win, then an entity like News Corp./DirecTV would create a powerhouse with guaranteed transmission rights on all three of the technologies used to distribute TV to the home. It will own broadcast stations, have must carry/retransmission rights on cable and satellite because of the broadcast licenses it holds, and own the largest satellite network. This is an immense power of distribution for a company that is vertically integrated into both broadcast and cable programming.

<sup>25</sup> One of the more ironic arguments offered by the cable operators feeds off of the observation that broadcast networks have carriage rights. They argue that even if cable operators foreclosed their channels to independent programmers, these programmers could sell to the broadcast networks. This ignores the fact that cable operators control the vast majority of video distribution capacity. There are approximately 60 channels per cable operator on a national average basis (Federal Communications Commission, 2002b, p. 10). There are approximately 8 broadcast stations per DMA on a national average basis (BIA Financial, 2002). Each broadcast station has must carry rights for one station. They can bargain for more, particularly in the digital space, but the cable operators control more stations there as well. In other words, if we foreclose 85 percent of the channels, the programmers will be able to compete to sell to the remaining 15 percent of the channels. Needless to say, this prospect does not excite independent programmers.

In the 1992 Cable Act, Congress recognized that the Federal government “has a substantial interest in having cable systems carry the signals of local commercial television stations because the carriage of such signals is necessary to serve the goals . . . of providing a fair, efficient, and equitable distribution of broadcast services.”<sup>26</sup> Congress also recognized that “[t]here is a substantial government interest in promoting the continued availability of such free television programming, especially for viewers who are unable to afford other means of receiving programming.”<sup>27</sup>

These governmental interests, as well as a finding that “[c]able television systems often are the single most efficient distribution system for television programming,” formed the original rationale behind Retransmission Consent. Because a majority of the country was receiving broadcast television service through cable, it was necessary to require that cable systems carry local broadcast signals. However, a merger between News Corp. and DirecTV would change the landscape against which Retransmission Consent was created. Given that this transaction will provide News Corp. with assets that no local broadcaster had in 1992 when Retransmission Consent was originally put in place – it will have a satellite distribution system capable of reaching a majority of the country – it seems that the original logic behind the rule is strained in the present circumstances. Not only will News Corp. own its own transmission system, but it also owns other programming that it bundles with its network programming, which may give it too much market power in negotiating cable and other carriage agreements. Congress should revisit the necessity of Retransmission Consent as it pertains to stations owned and operated by News Corp.

#### CONCLUSION

Consumers Union believes that the Department of Justice should impose substantial conditions on this deal which will otherwise be harmful to competition in the video programming market—harm that will be borne on the backs of consumers.

In addition, Congress should impose a new set of nondiscrimination requirements that would enable all media distributors and consumers to purchase video-programming and related services on an individual – as opposed to bundled – basis under terms that maximize competition and choice in the marketplace. Congress must reexamine the enormous market power and leverage that Retransmission Consent provides broadcast programmers – particularly one like News Corp. which, as a result of the merger with DirecTV, will own a new nationwide video distribution system (in addition to its over-the-air broadcast distribution system). And Congress should require cable and satellite operators to offer consumers the right to select the channels they want to receive at a fair price – in other words, require an a la carte program offering from all video distributors. Since the average household watches only about a dozen channels of video programming, this requirement could empower consumers to help discipline excesses in cable (or satellite) pricing, and could possibly spur more competition.

Congress must also carefully consider all the ramifications associated with the FCC’s June 2<sup>nd</sup> decision concerning the media ownership rules. Given that this decision was made

<sup>26</sup> Public Law 102-385, Section 2(a)(9).

<sup>27</sup> Public Law 102-385, Section 2(a)(12).

despite existing concentration in most of the nation's media markets, and given that the new rules do not provide for a public interest review of future mergers, Congress should enact legislation to reverse the FCC's decision.

If the FCC's decision is not reversed, the consolidation of news outlet ownership permitted by the new rules would likely result in the concentration of broadcast television station and newspaper ownership in a few hands within individual markets. The News Corp./DirecTV deal would look almost harmless in comparison to the avalanche of media mergers that could ensue. It is completely unfair to force American consumers to accept inflated cable rates and inadequate TV competition. But excess consolidation in the news media is even worse: the mass media provides Americans the information and news they need to participate fully in our democratic society. Without the ownership rules that effectively limit further consolidation in media markets, one company or individual in a town could control the most popular newspaper, TV and radio stations, and possibly even a cable system, giving it dominant influence and power over the content and slant of news. This could reduce the diversity of cultural and political discussion in that community.

The cost of excessive media consolidation and further media deregulation is very high. The cost of market failure in media markets is the price we pay when stories are *not* told, when sleazy business deals and bad accounting practices do *not* surface, when the watchdog decides that it would rather gnaw on the bone of softer news than chase down the more complicated realities that must be uncovered to make democracy function.



News from

**HERB KOHL**

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**FOR IMMEDIATE RELEASE:**

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June 18, 2003

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**Statement of U.S. Senator Herb Kohl  
Senate Antitrust Subcommittee Hearing on the News Corp.-DirecTV Merger**

A little more than a year ago, we sat in this room to examine EchoStar's attempt to acquire DirecTV. That deal would have created a monopoly in satellite television, and limited most consumers to only two choices for pay TV - the cable company and one satellite company. We opposed that merger, and, wisely, both the Justice Department and FCC decided to block it.

This year, it's News Corporation turn to try to acquire DirecTV, a deal presenting an entirely different set of issues. One of the world's largest media conglomerates - with holdings ranging from the Fox TV network, the Fox News Channel, Fox Sports Net, FX cable networks, the Twentieth Century Fox movie studio, 35 broadcast television stations, to newspapers like the *New York Post* and magazines like *TV Guide* - is seeking to acquire the DirecTV satellite system, the country's second largest television distribution system.

This combination of content holdings with worldwide distribution will create a media powerhouse of virtually unmatched size and scope. And, the overriding fear is that News Corp./DirecTV will take advantage of their global distribution system and must-have programming to raise prices and squeeze out competition.

Mr. Murdoch and Mr. Hartenstein will claim several benefits offered by this deal -- a stronger DirecTV, fortified by its corporate connection to News Corporation, deploying new technologies better able to compete with cable TV. But, for us, the crux of the matter is what most matter to consumers - the deal's likely effect on the ever rising prices paid by consumers for pay TV and on the choice and variety of programming available.

So, to convince us that this deal is truly in the public interest Mr. Murdoch and Mr. Hartenstein must answer some difficult questions. Will this deal create a vertically integrated media giant capable of raising the price of its programming and excluding other programmers from its powerful distribution network? Will this deal set in a motion a chain of mergers as content companies and distributors find it necessary to merge to compete with News Corp./DirecTV? And will this deal harm competition in the marketplace of ideas and further degrade the diversity of news, information and entertainment available to the American public?

- more -



# U.S. SENATOR PATRICK LEAHY

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VERMONT

Opening Statement Of Senator Patrick Leahy  
Hearing Before  
The Subcommittee On Antitrust, Business Rights, And Competition  
"The NewsCorp/DirecTV Deal:  
The Marriage Of Content And Global Distribution"  
June 18, 2003

I want to thank Chairman DeWine and Senator Kohl for holding this hearing today. This merger, and the larger issue of media consolidation, are very important to all of us, and I commend my colleagues on the Antitrust Subcommittee for continuing their fine tradition of bipartisan attention to important issues. We are becoming increasingly aware of the dangers of corporate consolidation, especially in the information and entertainment industries, where the First Amendment as well as the antitrust laws have significant roles to play. A hearing like this one is particularly timely and constructive, as we in the Senate strive to protect both the freedom of the marketplace and the freedom of speech.

No one in this room could have missed the firestorm of debate and outcry that accompanied the Federal Communications Commission's recent changes in the media ownership rules. I recognize that those changes do not touch directly upon the merger that we are addressing here today, but they are a tangible piece of the puzzle we are all trying so hard to solve. The Commerce Committee is thinking about it tomorrow. We will have another hearing on media concentration next week. Meanwhile the FCC continues to roll back the regulations that were designed to preserve a diversity of programming options and to ensure a variety of owners and a host of editorial choices and voices. The inevitable and escalating homogenization of programming can hardly inure to the benefit of viewers and listeners. I know this is true in rural States like Vermont, where we value our independence and we prize community-level debate and discussion, but I believe it is also true in every State and community across the land. When we add to that the likelihood that increasingly powerful media conglomerates can raise the prices consumers pay, at the same time that they can reduce the quality of their programming, the implications of unfettered media conglomeration to the American people and to our communities and to our society become troubling indeed.

I fear that is precisely the situation we find ourselves in today. As I wrote to the FCC when the rule changes were under consideration, there are those who argue that the increase in the number of media outlets has obviated the need for the rules limiting media ownership. The reality, of course, debunks this notion. While the number of media outlets has increased, ownership has become more concentrated. There are certainly no fewer opinions among the American people than in 1975 when the recently overturned standards were established, but there indisputably are fewer true avenues for their

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expression to meaningfully reach sizable segments of the population. In light of that incontrovertible fact, it seems illogical that the FCC would exacerbate a disturbing trend which is transforming the marketplace of ideas into little more than a corporate superstore.

The proposed deal between DirecTV and NewsCorp is not implicated by these rule changes, but it is an unavoidable truth that the atmosphere of concern created by the FCC's actions and attitudes will color the evaluation of all media deals. Each time that the FCC eases some restriction, we are assured that the "public interest" inquiry that the agency undertakes on such deals, along with the antitrust analysis conducted by the Justice Department, will ensure that consumers' legitimate interests are protected. Surely this merger is a deal to test the truth of this repeated assertion.

The questions raised about DirecTV and NewsCorp are hardly novel: When the nation's largest home satellite TV service is purchased by one of the world's largest media companies, it can come as no surprise that people are concerned about the choices consumers will really have. Will the new entity discriminate against other distributors, like cable companies, and especially against the small cable companies that serve many rural areas? Will this new entity discriminate against other content providers? Or will they favor NewsCorp's own popular programming – such as shows on the Fox TV network, Fox News Channel, and Fox sports channels?

I have two other major concerns, which are especially important to Vermont: the provision of local-into-local television to smaller Designated Marketing Areas (DMAs) and the roll-out of broadband service to under-served communities. Local-into-local television is critical to my state because it will allow satellite customers to get their local news and weather. Since July 2002, EchoStar has provided local-into-local television to its customers in Vermont. NewsCorp has assured me that they want to provide local-into-local TV to Vermont, but they have been unable to answer the question of *when* they will have the technological capacity. The same holds true for broadband to the under-served areas. Again, NewsCorp is hopeful they will be able to provide broadband to potential customers as soon as it can, but they have been unable to offer a timeframe.

This proposed merger raises many questions and concerns, and I appreciate all the witnesses being here today to help us address them. I look forward to hearing from you all.

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TESTIMONY OF ROBERT MIRON  
CHAIRMAN AND CHIEF EXECUTIVE OFFICER  
ADVANCE/NEWHOUSE COMMUNICATIONS

SUBCOMMITTEE ON ANTITRUST,  
COMPETITION POLICY AND CONSUMER RIGHTS

COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

JUNE 18, 2003

**Introduction**

Mr. Chairman, I am Bob Miron, Chairman of Advance/Newhouse Communications. Advance/Newhouse is a privately held company managing cable television systems that serve over two million households, principally in central Florida, and also in Alabama, California, Indiana, and Michigan.<sup>\*</sup> In addition to our company, I am testifying today on behalf of Cable One, Cox Communications, and Insight Communications.<sup>\*\*</sup> Together these companies serve nearly ten million cable television homes in thirty-one states. We thank you

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<sup>\*</sup> In addition to their cable interests, the Advance/Newhouse partners' other interests include Condé Nast Publications and a number of daily and weekly newspapers and business journals.

<sup>\*\*</sup> The majority shareholder in Cox Communications (CCI-NYSE) is Cox Enterprises Inc., which also holds a majority interest in Cox Radio (CXR-NYSE) and privately owns newspapers, television stations, Internet sites and automobile auctions. Cable One is owned by the Washington Post Company, which is a diversified media and education company whose other principal operations include newspaper and magazine publishing, television broadcasting, electronic information services, test preparation, and educational and career services. Insight Communications delivers bundled interactive services to customers in mid-sized communities of the four contiguous states of Illinois, Kentucky, Indiana and Ohio, delivering digital video and high-speed data access, as well as telephone services in selected markets.

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Mr. Chairman, and we thank Senator Kohl and the members of the Subcommittee for this opportunity.

As the strongest and most experienced provider of direct broadcast satellite service worldwide, News Corp. brings management expertise and technology to DirecTV. Certainly News Corp. brings financial resources. And certainly Mr. Murdoch is a successful businessman. No doubt News Corp.'s acquisition of a controlling interest in DirecTV can have benefits to competition.

What we find troubling is that the acquisition will give News Corp. unique and unprecedented power and incentive to raise the cost to consumers on all three multichannel TV platforms – cable, DirecTV, and EchoStar/DISH. In our view this power, if not checked by the imposition of conditions on the transaction, outweighs any benefits. The risk is magnified by the possibility, and perhaps even the likelihood, that this transaction will be followed by a similar consolidation involving EchoStar. It is not the size of News Corp. combined with DirecTV that concerns us. It is the market effects of the unique combination of News Corp.'s powerful programming assets with a national DBS platform that concern us.

News Corp. has recognized the existence of certain problems, and has proposed conditions, to be set forth in a consent decree, to deal with them. Nevertheless, our review has convinced us that News Corp.'s conditions, while helpful, are in no way adequate to the task at hand. Therefore, we are asking the Justice Department and FCC to review this acquisition with

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care and to approve it only when both agencies are satisfied that adequate competitive and behavioral safeguards are in place.

**This Transaction Presents Issues Never Before  
Confronted by the Justice Department and the FCC**

Once this transaction is approved, News Corp. will control a national multichannel distribution system, one and sometimes two or more local broadcast stations in virtually every major television market, a broadcast network, a suite of cable networks (including both a national and regional sports networks), and studio assets. With over eleven million subscribers and a national footprint, DirecTV alone is already one of the top three video distributors, including both cable and DBS. And it will have the ability to grow much larger without the territorial restrictions and capital investment barriers faced by cable competitors.

Today, there are vertically integrated companies that combine powerful programming assets with cable system ownership. Those companies are subject to legislation, FCC rules and consent decree provisions that limit their exercise of power. But no cable company currently has the potential to serve more than about a third of American homes. None comes close to the geographic reach of DirecTV, which is a competitive presence in every television market. And none currently owns broadcast stations inside its cable markets, while News Corp. owns and operates thirty-five stations within DirecTV's national service area, and a "big four" television network. That is why the News Corp./DirecTV transaction presents issues never before

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considered by the Justice Department and the FCC, and why it cannot be dealt with in summary fashion.

**The Transaction Will Give News Corp. New Power and Incentive to Raise Prices on All Three Platforms – Cable, DirecTV and EchoStar**

From my vantage point in the cable industry, I can tell you that it is already hard enough to negotiate with the four companies that combine ownership of broadcast networks, broadcast stations and cable networks. Retransmission consent negotiations inevitably involve not just carriage of broadcast stations, but how much cable operators will pay for the broadcast stations' affiliated cable networks, and how many new affiliated networks they will carry. Inevitably cable operators face demands for carriage of these affiliated channels on their most-watched tier of programming, so that all subscribers have no choice but to pay for them. Like network affiliated broadcast stations, regional sports networks are "must have" programming. They present much the same set of negotiating problems for us, and News Corp. operates by far the largest collection of regional sports networks.

News Corp. currently owns thirty-five broadcast stations, including nine in the top ten markets and sixteen in the top twenty markets. News Corp. currently owns two stations in nine of those markets, including New York, Los Angeles and Chicago. News Corp. controls regional sports networks serving eighteen regions. These regions include ten of the top twenty television markets. In each of the eighteen regions, control of the regional sports network is combined with ownership of at least one Fox-affiliated broadcast station. In five television markets News Corp.

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combines duopoly ownership of broadcast stations with control of a regional sports network. Those markets are Los Angeles, Dallas-Ft. Worth, Tampa-St. Petersburg, Minneapolis-St. Paul, Phoenix and Orlando-Daytona. Because programmers negotiate with cable operators on a company-wide basis, News Corp.'s leverage in key markets affects prices nationally.

Today both EchoStar and DirecTV approach their negotiations with programmers from much the same point of view as cable does, and that is what makes today's marketplace workable. Once DirecTV becomes, effectively, a partner of the News Corp. stations and networks, cable's and EchoStar's negotiating leverage will be lost. If we fail to reach carriage agreements, we will be granting our competitor de facto exclusive carriage of very desirable programming. That is not acceptable, and we will be forced to concede. So will EchoStar. Prices will go up for DirecTV customers, EchoStar customers, and cable TV customers. Independent observers share our concerns. For example, according to Robert Kaimowitz, Chief Executive of the investment fund Bull Path Capital Management, "my sense is that the major purpose for News Corporation controlling DirecTV is to use it as a tactical weapon against the cable companies to get them to pay up for its proprietary programming." And Thomas Watts, of SG Cowen, believes it "likely that News Corp. also would exercise its leverage as a content provider and make money in all markets by raising programming costs for everyone."

We believe the impact will be substantial nationally. It will be even more severe for small and mid-sized cable operators, many of whom operate in smaller markets and rural areas, and who typically pay higher prices for programming than does DirecTV.

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Our view is also confirmed by the analysis performed at our request by Dr. William Rogerson, formerly chief economist at the FCC and currently Professor of Economics at Northwestern University. Professor Rogerson's analysis is Attachment A to my statement. We expect this study to be rigorously examined by the independent economists at the Antitrust Division and the FCC, and we believe it will stand up. As Professor Rogerson summarizes his findings:

“The proposed merger between News Corp. and DirecTV will give News Corp. both the incentive and ability to charge higher programming prices to MVPDs that are rivals of DirecTV. In the short run this will harm consumers because these price increases will be passed through to them in the form of higher subscription prices. In the long run, price increases to MVPDs will harm competition at the MVPD level -- especially in less dense regions of the country where the business case for multiple MVPDs is more tenuous . . .” (Appendix A, page 33)

**News Corp.'s Proposed Consent Decree is Inadequate**

News Corp. has proposed two conditions, to be set forth in a consent decree. They have proposed to comply with the FCC's program access rules as though DirecTV were a cable system. They also have proposed to subject transactions between DirecTV and News Corp.'s Fox broadcast stations and cable networks to review by an independent audit committee of DirecTV's board.



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**Program Access**

First and most important, the program access rules do not prevent News Corp. from using the additional power it will gain from control of DirecTV to raise rates for cable television and EchoStar, so long as they avoid “discriminating” by also raising rates to DirecTV. We believe they have the incentive to do just that. Our opinion is confirmed by Dr. Rogerson’s study and is widely shared by Wall Street analysts. We believe this opinion also will be shared by the FCC and Antitrust Division, so long as the transaction receives careful study.

Second, as we understand their public statements and filings, News Corp. has not proposed subjecting its broadcast station retransmission consent negotiations to the nondiscrimination requirements of the program access rules. Broadcast stations are not included in the FCC rules because when the rules were adopted, cable systems were prohibited from owning broadcast stations in their service areas. Although the cable/broadcast crossownership rule is no longer in place, no such ownership exists today, and we believe the issue of nondiscriminatory treatment of competitors EchoStar and DirecTV would arise if any such acquisition were proposed. The Fox broadcast affiliates are the “big dogs” of News Corp.’s programming complex (along with the regional sports networks). Failure to include them in the program access commitment greatly reduces its value.

**Audit Committee**

Advance/Newhouse is privately held, and I, personally, do not have much experience with public company audit committees. I have consulted with my colleagues who do have

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relevant experience, and we have also sought advice from Lynn Stout, Professor of Law at UCLA Law School and formerly Director of the Georgetown-Sloan Project on Business Institutions of the Georgetown University Law Center. Her affidavit, already submitted to the FCC, is Attachment B to my testimony. Our conclusion is that, at most, an audit committee could try to satisfy itself that Fox is not overcharging DirecTV in comparison to EchoStar and cable systems. Even that would require Fox to grant DirecTV access to information about rates, terms and conditions in contracts between Fox and DirecTV's competitors, which under industry practice normally would be subject to confidentiality agreements

In any event if, as News Corp. has promised, the same rates are charged to cable, DirecTV and EchoStar, as we understand it no audit committee, no matter how conscientious, can identify the premium to the Fox networks from all three platforms resulting from Fox's control of DirecTV. Nor, as we understand it, would Sarbanes-Oxley or corporate law impose any requirements in this regard. As Professor Stout says,

“. . . [T]ransactions between parent and subsidiary corporations often give rise to common economic benefits . . . Delaware law does not require a controlling shareholder to share these common benefits with the subsidiary or the subsidiary's noncontrolling shareholders, because it does not treat a failure to share as a detriment to minority shareholders.” (Attachment B, page 6.)

Audit committees are designed to find harm to shareholder interests. Here the harm is to the marketplace and consumers.

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Hopefully these issues will be fully examined as the government review process goes forward.

**Conclusion**

The News Corp. acquisition of DirectTV presents new issues never before considered by the Justice Department and the FCC. If the agencies get it wrong, there will be adverse impacts on consumers, including higher cable rates for popular programming. The consumer impacts could be greatly magnified if, as we believe likely, a similar consolidation involving EchoStar should emerge.

Therefore News Corp.'s acquisition can be in the public interest only if appropriate conditions can be constructed, in addition to those already proposed, to limit the adverse effects on consumer prices for DBS and cable TV. We believe appropriate conditions can be found. We are prepared to join in the search. We urge the Justice Department and FCC to take a careful look at this transaction. We urge the Subcommittee to continue its oversight.

**Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, DC 20554**

In the Matter of: )  
)  
General Motors Corporation, Hughes )  
Electronics Corporation, and the )  
News Corporation Limited ) MB Docket No. 03-124  
Application To Transfer Control Of FCC )  
Authorizations And Licenses Held By )  
Hughes Electronics Corporation )  
To The News Corporation Limited )

**AN ECONOMIC ANALYSIS OF THE COMPETITIVE EFFECTS  
OF THE TAKEOVER OF DIRECTV BY NEWS CORP.**

My name is William P. Rogerson. I am a professor of economics at Northwestern University. In 1998-99 I served as Chief Economist at the Federal Communications Commission ("Commission"). I have published numerous academic articles on industrial organization, regulation, the economics of contracts, and telecommunications. I have served as chairman of the Department of Economics at Northwestern and am currently Co-Director of the Center for the Study of Industrial Organization and Director of the Program for Mathematical Methods in the Social Sciences at Northwestern. I served as the outside economic expert for the Federal Trade Commission when it reviewed the AOL-Time Warner merger, and also served as the economic expert for the National Association of Attorneys General to support its analysis of the DirecTV EchoStar merger. A copy of my curriculum vitae is attached at Exhibit I.

**INTRODUCTION**

The proposed takeover of DirecTV by News Corp. can be classified as a vertical merger because News Corp. operates in “upstream” industries that provide programming<sup>1</sup> to the “downstream” multichannel video programming (“MVPD”) industry, in which DirecTV provides direct broadcast satellite (“DBS”) service. News Corp. owns thirty-five local broadcast television stations across the country. As such, News Corp. supplies the “retransmission consent” rights that authorize MVPDs to retransmit local over-the-air broadcast signals to their subscribers. News Corp. is also the producer of some of the most popular and heavily watched subscription video programming in the country, including Fox News Channel, FX, Fox Movie Channel, Speed Channel, Fox Sports Networks, and the Fox Regional Sports Networks (“RSNs”). DirecTV is one of the three largest MVPD in the country, competing with cable operators for the delivery of video programming in every local market nationwide.

A large body of scholarship using the methodologies of modern industrial organization theory has shown that, in oligopolistic market structures, circumstances exist where vertical mergers can exacerbate horizontal market power and create competitive harms.<sup>2</sup> I believe that the facts of this case fit these circumstances. In particular, I believe that there are two distinct

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<sup>1</sup> I consider both local broadcast television retransmission consent and the subscription video programming channels as “programming” inputs below.

<sup>2</sup> See, e.g., Michael H. Riordan & Steven C. Salop, *Evaluating Vertical mergers: A Post-Chicago Approach*, 63 Antitrust L.J. 513 (1995); Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals’ Costs to Achieve Power Over Price*, 96 Yale L.J. 209 (1986); Janusz A. Ordover, Garth Saloner, and Steven C. Salop, *Equilibrium Vertical Foreclosure*, 80 American Economic Review (1990); Oliver Hart and Jean Tirole, *Vertical Integration and Market Foreclosure*, *Brookings Papers on Economic Activity: Microeconomics 1990* (1990); Ilya R. Segal and Michael C. Whinston, *Exclusive Contracts and Protection of Investments*, 31 Rand Journal of Economics (2000).

but related economic reasons to expect that the merged entity will raise the prices that it charges for programming to MVPDs that are rivals of DirecTV.

First, I believe that News Corp. will have an increased *incentive* to raise prices because raising the prices it charges to rival MVPDs will increase the profits of DirecTV. This explanation of why a vertically integrated supplier will raise prices to rival downstream firms is typically referred to as the incentive to “raise rivals’ costs” in the economics and antitrust literature and is generally viewed as the most standard explanation for why vertical mergers can cause price increases. It is an issue that the Commission has considered and addressed many times before and provides the underlying rationale for “program access” rules that prohibit programmers who are vertically integrated with cable MSOs from discriminating against rival MVPDs.<sup>3</sup>

Second, I believe that News Corp. will have an increased *ability* to raise prices to rival MVPDs because its bargaining power will be increased. News Corp.’s “bargaining power” is based on its ability, when negotiating with an MVPD, to credibly threaten to withhold programming from the MVPD. This threat will be less costly to News Corp. (and, therefore, more credible) after the merger because the cost of lost subscription and advertising revenues from withholding programming will be to some extent offset by the increased profits that DirecTV will earn when a rival MVPD is denied this programming. The merger will give News

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<sup>3</sup> I understand that News Corp. also controls the leading electronic program guide (“EPG”) technology. EPGs essentially act as the operating system for digital set-top boxes in a cable system. I understand that the Department of Justice believes EPGs are a relevant antitrust product market and there are numerous barriers to entry into that market. Although I will not discuss this market in further detail in this paper, I believe that News Corp. may also have a similar sort of incentive to raise rivals’ costs in this market.

Corp. the ability to obtain higher prices in its negotiations with program purchasers to the extent that it can more credibly threaten to withhold programming from DirecTV's rivals.

The exclusionary dangers of a "raising rivals' costs" strategy are an important concern in this merger. Indeed, they are significant enough in and of themselves to warrant the Commission's attention. The danger of enhancing News Corp.'s bargaining power is a more novel issue that I do not believe the Commission has ever explicitly addressed before in its evaluation of the competitive harms of vertical integration. I believe this second danger is also significant enough to merit close scrutiny by the Commission.

It is also important to note that both of these effects will be particularly serious in less dense regions of the country served by small to medium sized cable systems. This is because raising the price of programming or withdrawing programming from these firms is more likely to drive them entirely out of the market. This will increase both News Corp.'s incentive to raise prices and withdraw programming and the bargaining power it can wield by threatening to withdraw programming. Therefore the merger is most likely to cause significant price rises in less dense regions of the country served by small to medium sized cable systems.

As I explain in more detail below, News Corp.'s increased incentive and ability to raise prices will cause two important harms to consumers. In the short run, price increases to MVPDs will harm consumers because they will be passed through in the form of higher subscription prices. In the long run, price increases to MVPDs will harm competition at the MVPD level -- especially in less dense regions of the country where the business case for multiple MVPDs is more tenuous -- as DirecTV's rivals will be driven out of business or fundamentally weakened. In those markets, DirecTV will eventually be able to increase prices even more.

I understand that News Corp. has, as part of its application for merger approval, offered to abide by the same non-discrimination rules that would apply to a cable network programmer that is vertically integrated with a cable system. I have a number of serious reservations regarding the adequacy of this proposed condition to address the foregoing harms. First, News Corp.'s offer to abide by nondiscrimination conditions applies only to the prices it charges for cable network programming and does not apply to the prices it charges for retransmission consent for local broadcast signals. Therefore, it leaves a major aspect of the problem completely unaddressed. Second, since the proposed condition expressly allows quantity discounts, it places very little constraint on the prices that News Corp. could charge smaller cable systems. Finally, even if these problems could be solved, the proposed condition only requires that News Corp. charge the *same* prices to all MVPDs. News Corp. could comply fully with the condition and still charge high prices to its rivals simply by charging equally high prices to DirecTV.

My analysis is organized as follows. Section I explains how local television station signals are both unique and desirable and how there are no adequate substitutes for them as a result of government regulations relating to retransmission consent, such that News Corp. would have the ability to significantly harm rival MVPDs by either withholding this programming or by raising its price. Section II explains how it is similarly difficult for MVPDs to find substitutes for the regional sports programming offered by News Corp., such that News Corp. would have the same ability to significantly harm rival MVPDs by withholding this programming or by raising its price.



Section III explains why News Corp. will have an increased ability to increase prices for these programming inputs following the merger. Section IV explains why News Corp. will have an increased incentive to raise prices following the merger. Section V makes a few brief comments comparing the two theories. Section VI describes the harms to consumers that will result. Section VII explains why the non-discrimination condition proposed by News Corp. is inadequate to address the potential harms I have identified. Section VIII presents a brief and preliminary discussion of conditions to remedy these harms. Finally, Section IX draws a brief conclusion.

**I. RIVAL MVPDs WOULD BE HARMED IF THEY WERE DENIED RETRANSMISSION CONSENT OF NEWS CORP.'S LOCAL BROADCAST STATIONS**

A vertically integrated programmer will only be able to raise prices to rival MVPDs if it controls “must have” programming that is highly desired by consumers and for which no good substitutes exist. In this section I will argue that the signals of News Corp.’s local broadcast stations meet these criteria. Furthermore, there is no substitute for such programming primarily because government regulation protects these stations from competition. The next-best substitute for the signal of a local broadcast station that is affiliated with a particular network is the signal of an out-of-region affiliate of the same network. Government regulations allow the local network affiliate to prohibit MVPDs from retransmitting this next-best substitute. For these reasons, I believe that News Corp. could harm rival MVPDs by denying them retransmission consent for News Corp.’s local broadcast stations.

**A. Background**

Cable operators and other MVPDs retransmit the signals of local broadcast stations as part of their multichannel video programming package. The 1992 Cable Act allows local broadcasters to elect either “must carry” or “retransmission consent” status with each MVPD in their broadcast area. If a broadcaster elects “must carry” status with respect to a particular MVPD, then the MVPD must carry the signal of the local broadcaster at no charge to the broadcaster. If a broadcaster elects “retransmission consent” status with respect to a particular MVPD, the local broadcaster has the right to deny the local MVPD the right to retransmit its signal and is allowed to seek to negotiate consideration for the right to retransmit the signal.

Most commercial stations elect retransmission consent status and negotiate some consideration for the right to retransmit their signal. At the moment, I understand that most stations negotiate a “payment in kind” rather than a cash payment. Many stations are owned by parent companies that also own cable programming interests. In these cases, the parent company typically negotiates agreements for the MVPD to carry (and pay for) affiliated cable programming.<sup>4</sup>

However, it is reportedly becoming more common for local broadcasters to attempt to negotiate cash payments (on a per subscriber per month basis) for retransmission consent.

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<sup>4</sup> The American Cable Association has filed a petition for inquiry with the Commission asking it to investigate retransmission consent practices, which describes retransmission consent negotiations in more detail. See American Cable Association, *Petition for Inquiry into Retransmission Consent Practices* (“Retransmission Consent Petition”), October 1, 2002, and American Cable Association, *Petition for Inquiry into Retransmission Consent Practices First Supplement* (“Retransmission Consent Petition First Supplement”), December, 2002. See also American Cable Association, *Reply Comments In the Matter of 2002 Biennial Regulatory Review and Review of the Commission’s Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996* (“ACA Reply Comments”), MB Docket No. 02-277, February 1, 2003.

ABC/Disney, for example, has reportedly offered a number of MVPDs the option of paying \$.70 per subscriber per month as an alternative to carrying certain Disney cable channels. News Corp. has asked for a payment of \$.65 per subscriber per month to carry Fox and \$.30 per subscriber per month to carry UPN as an alternative to carrying certain News Corp. Channels. Gannett Broadcasting Group has apparently begun to ask for cash payments of between \$.18 and \$1.00 per subscriber per month with no other alternative being offered.<sup>5</sup> These represent very significant dollar payments and are comparable in size to the prices that programmers charge for marquee -- and even some premium -- channels.<sup>6</sup>

In a recent news interview Lachlan Murdoch reported that he plans to begin asking for payments for retransmission consent. He is quoted as saying:

We're going to have to work with MSOs (multiple system operators) on a payment for the retransmission of the broadcast signal, which, frankly, is what's fair because of the ratings broadcast television drives. Broadcasters need a healthy revenue stream to offset rising costs.<sup>7</sup>

Therefore, although we may not normally think of local broadcast signals as a type of programming that is sold to MVPDs for a positive price, this is in reality the case. Furthermore,

<sup>5</sup> See *ACA Reply Comments*, Exhibit D, "Examples of Retransmission Consent Abuse Reported by ACA Members, November 1, 2002-January 31, 2003."

<sup>6</sup> For example, ESPN currently charges \$1.30 per subscriber per month, USA Network charges \$.40 per subscriber month, and Comedy Central charges between \$.09 and \$.16 per subscriber per month. Even Starz!, one of the fastest growing premium networks, charges only \$.235 per subscriber per month. See R. Thomas Umstead, *Sure it's a Spring Rite, But Ops Say: Not Right*, *Multichannel News*, April 21, 2003, at 1 (providing numbers for ESPN); Kagan Cable Program Investor, February 20, 2003, at 5 (providing numbers for USA); Linda Moss & Mike Farrell, *Viacom Buys Custody; Comedy Central Joins MTVN Stable*, *Multichannel News*, April 28, 2003 at 1 (providing numbers for Comedy Central); Kagan Cable Program Investor, April 16, 2003, at 11 (providing numbers for Starz!).

<sup>7</sup> See *Lachlan Murdoch's Lead: Enhancing TV Stations and Family Biz*, *Merimigas on Media*, March 18, 2003

the fact that local broadcasters derive a majority of their revenue from advertising sales does not stop them from taking advantage of their control over retransmission rights to also negotiate positive prices for retransmission consent.

**B. News Corp's Local Station Signals Are "Must Have" Programming**

MVPDs view the local broadcast signals of the affiliates of the four major over-the-air broadcast networks, including the Fox Network owned by News Corp., as "must have" programming that they must carry in order to compete effectively for customers. In its *Retransmission Consent Petition* the American Cable Association summed up the situation as follows:

No one can seriously question who holds the power when a small cable operator must deal with . . . Fox/News Corp. . . . The network owners know that local network signals are essential services for small cable operators.<sup>8</sup>

To some extent, therefore, the power of News Corp.'s stations is the power of their programming. Fox network programming includes such popular items as the World Series and other Major League Baseball post-season games, the 16 National Football Conference games in the National Football League, and shows like "The Simpsons," "24" and "American Idol."

The power of a local broadcast station that is an affiliate of one of the major networks would be dramatically reduced if MVPDs were able to negotiate with out-of-region affiliates of the same network for the right to retransmit their signals. This, however, is prevented by government regulations such as the "Network Non-Duplication Rule" and the "Syndicated Exclusivity" rule. Therefore, to some extent, the power of local broadcast stations is enhanced by government regulation.

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<sup>8</sup> See *Retransmission Consent Petition* at 11.

Moreover, News Corp. exercises this power in local markets nationwide. News Corp. owns 35 broadcast stations,<sup>9</sup> and its owned and operated (“O&O”) broadcast station group has the second largest reach, in terms of households, out of all station owners in the U.S.<sup>10</sup> This means that News Corp.’s power over local broadcast signals currently reaches into more local markets than almost anyone else. And, the Commission’s recent relaxation of the national broadcast ownership cap from 35 percent to 45 percent will permit News Corp. to even further expand its ownership of local stations. I understand that News Corp. has already purchased more local stations than the rules allowed under the old cap.<sup>11</sup> Now that the cap has been relaxed further, it is very likely that News Corp. will expand its holdings to the extent allowed by the new cap.<sup>12</sup>

**C. Customer Response to Temporary Withdrawals of Retransmission Consent from MVPDs Confirms That Fox Stations Are “Must Have” Programming**

I believe it is instructive to look at the marketplace today to determine whether the foregoing conclusions can be verified. There have been a number of well-publicized incidents in the last few years where News Corp. or some other local broadcast station has withdrawn retransmission consent from an MVPD during negotiations. The evidence suggests that significant numbers of customers leave the MVPD that can no longer offer the local station and,

<sup>9</sup> See *Top 25 Television Groups*, Broadcasting & Cable, April 8, 2002, at 48.

<sup>10</sup> See *Less is More as Viacom Retakes Top Spot*, Broadcasting & Cable, April 8, 2002, at 46.

<sup>11</sup> See Frank Ahrens, *FCC Rule Fight Continues in Congress*, Newsbytes, June 4, 2003 (noting that Fox already owns stations in excess of the FCC’s former ownership cap, reaching 37% of households); David Folkenflik, *FCC Opens Door to Survival For Biggest Media*, Baltimore Sun June 4, 2003.

<sup>12</sup> See *Some See Opportunity For Deals in FCC Rules, Others See Legal Action*, Communications Daily, June 4, 2003, at 5 (quoting Legg Mason analyst Blair Levin).

instead, switch to another MVPD that can. Furthermore, MVPDs that are still able to offer the local station typically heavily advertise this fact in an attempt to steal customers away from the affected MVPD.

In a recent case from the Washington, D.C. area, News Corp. withheld the signal of Fox station WTTG-TV during a retransmission consent negotiation.<sup>13</sup> The dispute arose near the beginning of the NFL playoffs and subjected Cox Communications to significant negative customer relations in several markets.<sup>14</sup> During the course of negotiations, satellite providers “profit[ed]” from the disruption of service, aggressively marketing themselves to consumers as an alternative to Cox.<sup>15</sup> Eventually, Cox Communications agreed to News Corp.’s demands and the signal was restored. In other cases of which I am aware, there have been similar results. The lack of available substitutes makes News Corp.’s local stations “must have” programming for MVPDs.

**D. Customer Response to Local-to-Local Offerings of DBS Providers Confirms That Fox Stations Are “Must Have” Programming**

DirecTV and EchoStar claim that their ability to attract customers away from cable increased significantly when they were able to begin offering local broadcast signals,<sup>16</sup> and this provides more evidence that local signals are “must have” programming. In filings with the

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<sup>13</sup> See *Comments of Cox Enterprises, Inc.*, MB Docket No. 02-277, at 45 (January 2, 2003) (“*Comments of Cox*”).

<sup>14</sup> See Linda Moss, *Some Subs Who Lost Fox Get Refunds From Cox*, Multichannel News, January 17, 2002, at p. 3.

<sup>15</sup> Kristina Stefanova, *Satellite Soaring: Fox-Cox Flap Also Sells Antennas*, The Washington Times, January 4, 2000 at p.B8.

<sup>16</sup> See Satellite Home Viewer Improvement Act, Pub. L. No. 106-113, 113 Stat. 1501 (1999) (“SHVIA”) (codified at 47 U.S.C. § 338, “Carriage of Local Television Signals by Satellite Carrier”).

Commission, EchoStar reports that the addition of local channels has made DBS more competitive with incumbent cable providers and has led to an increase in DBS subscribership and a restraint on cable prices,<sup>17</sup> and DirecTV reports that its overall subscriber levels have increased by 20 percent due to the provisioning of local broadcast channel service.<sup>18</sup> Such evidence confirms that local broadcast signals generally are “must have” programming.

The Commission itself has recognized that the offering of local channels, which it calls “valuable programming,” has allowed DBS providers to make significant gains in the MVPD market:

DBS providers have made significant progress as competitors to cable, capturing 18 percent of MVPD subscribers, due in part to authority granted by SHVIA to DBS operators to distribute local broadcast television stations in their local markets. Indeed, we believe that the marked growth of DBS since the enactment of SHVIA provides an informative example of the impact on competition in the distribution of video programming when marketplace participants gain access to valuable programming to which they were previously denied.<sup>19</sup>

**II. RIVAL MVPDs WOULD BE HARMED IF THEY WERE DENIED NEWS CORP. REGIONAL SPORTS PROGRAMMING**

News Corp.’s regional sports networks are also “must have” programming that are highly desired by consumers and for which no good substitutes exist. This means that News Corp.

<sup>17</sup> *Annual Assessment of the Status of Competition in the Market For the Delivery of Video Programming, Ninth Annual Report*, MB Docket No. 02-145, at ¶ 61 (2002).

<sup>18</sup> *Annual Assessment of the Status of Competition in the Market For the Delivery of Video Programming, Eighth Annual Report*, 17 FCC Rcd 1244, 1273-1274 ¶ 59 (2001) (“*Eighth Annual Video Competition Report*”).

<sup>19</sup> *In the Matter of (i) Implementation of the Cable Television Consumer Protection And Competition Act of 1992 (ii) Development of Competition and Diversity in Video Programming Distribution: Section 628(c)(5) of the Communications Act and (iii), Sunset of Exclusive Contract Provision, Report and Order*, 17 FCC Rcd 12124, 12144 ¶ 46 (2002) (“*Sunset Extension Order*”).

could also harm its rivals by pursuing exclusionary or cost-raising strategies with respect to this programming.

**A. Regional Sports Programming is “Must Have” Programming**

The Commission has generally concluded that a significant amount of cable programming is of the “must have” variety and has specifically given RSNs as an example of such “must have” programming. For example, in its order extending the Sunset of Program Access Rules (*Sunset Extension Order*) the Commission found that:

given the unique nature of cable programming, there frequently are no good substitutes available for . . . [regional sports services, which] are considered ‘must have’ programming by competitive MVPDs and the subscribers they serve . . . .<sup>20</sup>

To explain its conclusion regarding regional sports programming the Commission noted that this programming is by its very nature unique, since networks typically purchase exclusive rights to show sporting events:

Competitive MVPDs argue that regional or local sports programming presents a special problem because it is unique programming. Commenters argue that local sports cannot be duplicated by competing MVPDs or acquired from alternative sources, even if the cost of doing so were not an issue. RCN asserts that for the fan who wishes to see a Washington Redskins game, the alternative of a local NBA or NHL game, or even a distant NFL contest, is not an acceptable substitute. . . These commenters contend that because local sports programming is so highly desired by subscribers, its unavailability imposes an unusually significant competitive harm [footnotes omitted].<sup>21</sup>

To support its conclusion that regional sports programming is “must have” programming the Commission cites data provided by DirecTV and EchoStar showing that they have significantly lower subscribership in Philadelphia as compared to other large cities and noting DirecTV’s and EchoStar’s claim that “this is directly attributable to their inability to access Comcast

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<sup>20</sup> *Id.* at 12139 ¶ 34.

<sup>21</sup> *Id.* at 12137 ¶ 29.



SportsNet.”<sup>22</sup> In its most recent working paper the Commission’s Office of Plans and Policy concludes that:

Regional sports programming in particular has been, and continues to be, an important segment of programming for all video program providers. According to a 2000 survey, between 40 and 58 percent of cable subscribers would be less likely to subscribe to cable service if it lacked local sports. Cable overbuilders have frequently noted that access to sport programming is so essential to the success of a cable system that many operators will pay exorbitant prices and agree to entertain other less attractive business arrangements just to obtain it.<sup>23</sup>

Simply put, sports fans feel there is no good substitute for watching their local and/or favorite team play an important game.

**B. News Corp. Holds a Powerful Position in Local Sports Programming**

It is widely recognized, to quote the Commission’s own Office of Plans and Policy, that “regional sports distribution is dominated by Fox Sports Net,”<sup>24</sup> which is of course owned by News Corp. Today, News Corp. owns interests in 19 regional sports networks (“RSNs”) reaching three-quarters of all television households.<sup>25</sup> The Fox RSNs carry 67 of the 80 professional MLB, NBA, and NHL teams.<sup>26</sup> The RSNs produce over 4,500 professional live events annually.<sup>27</sup> News Corp. also controls the national broadcast rights to NFC professional

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<sup>22</sup> *Id* at 12139 ¶ 33 n.107.

<sup>23</sup> Jonathon Levy, Marcelino Ford-Livine, and Anne Levine, *Broadcast Television: Survivor in a Sea of Competition*, Office of Plans and Policy Working Paper 37, September 2002, at 124 (“*Broadcast Television OPP Working Paper*”).

<sup>24</sup> *See Broadcast Television OPP Working Paper* at 125.

<sup>25</sup> *See Application* at Attachment F. However, News Corp. claims 21 RSNs on its website. *See* [www.newscorp.com/management/fsn.html](http://www.newscorp.com/management/fsn.html).

<sup>26</sup> *See* [www.newscorp.com/management/fsn.html](http://www.newscorp.com/management/fsn.html).

<sup>27</sup> *See* [www.newscorp.com/management/fsn.html](http://www.newscorp.com/management/fsn.html).

football and major league baseball games as well as NASCAR races.<sup>28</sup> And, News Corp. controls several major packages of college basketball and football games.<sup>29</sup> Therefore it is clear that a very large fraction of the most desirable local sports programming is controlled by RSNs owned in whole or in part by News Corp.

**C. Customer Response to Temporary Withdrawals of Local Sports Programming from MVPDs**

There have been a number of well-publicized incidents in the last few years where News Corp. or some other program supplier has withdrawn regional sports programming from an MVPD during negotiations over prices. These incidents provide us with a sort of “natural experiment” that we can use to measure the extent to which News Corp. could damage rival MVPDs by withdrawing regional sports programming from them. The evidence suggests that significant numbers of customers leave the MVPD that can no longer offer local sports and, instead, switch to another MVPD that can. Furthermore, the MVPD that is still able to offer the local sports programming is apparently well aware that this creates an enormous strategic advantage for it and its typical response is to heavily advertise the fact that it still offers the local sports programming in an attempt to steal customers away from the affected MVPD.

For example, in Minnesota, Fox Sports Net North was cut from more than 150,000 Time Warner Cable homes when the two could not come to terms. EchoStar distributors reported their business “tripled as soon as [FSN] was taken off cable.”<sup>30</sup> DirecTV officials likewise reported

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<sup>28</sup> See [www.newscorp.com/management/fsn.html](http://www.newscorp.com/management/fsn.html).

<sup>29</sup> See [www.newscorp.com/management/fsn.html](http://www.newscorp.com/management/fsn.html).

<sup>30</sup> Judd Zulgadd, *Cable Squabble Leaves Sports Fans Pondering Options*, Star Tribune, Jan. 27, 2003, at 1A.

increases in sales.<sup>31</sup> And, when YES network failed to reach a carriage deal with Cablevision, DirecTV immediately began to advertise heavily in Cablevision markets to pick off subscribers.<sup>32</sup> During the dispute, DirecTV's rate of signing up new customers increased 100 percent.<sup>33</sup> Cablevision lost at least 30,000 customers to DirecTV as a result.<sup>34</sup>

### III. THE MERGER INCREASES THE ABILITY OF NEWSCORP TO RAISE THE PRICES IT CHARGES FOR PROGRAMMING

In this section, I will explain how the merger increases the ability of News Corp. to raise the prices it charges for its "must have" programming. Essentially, the merger will enhance News Corp.'s ability to walk away from the bargaining table with an unaffiliated MVPD because it will be able to more credibly threaten to withdraw programming from the MVPD. After the merger, the cost of such a strategy will go down because the loss of programming revenues from the rival MVPD will to some extent be offset by the increased profits of DirecTV. Moreover, News Corp. will be able to engage in temporary withdrawals of programming from MVPDs that refuse to go along with higher prices. As I show below, the costs of such a "temporary withdrawal" strategy to News Corp. will be even smaller, but the damage to MVPDs will be

<sup>31</sup> *Id.* Such examples are not uncommon. In 2001, when Time Warner Cable refused to accept Fox Sports West terms for Dodgers games, DirecTV stepped right in and advertised free equipment and installation to Time Warner subscribers. Linda Haugsted, *Subtracting Sports: Licensing Hassles Lead to Cable Drops*, Multichannel News, July 2, 2001, at 1.

<sup>32</sup> In an undated open letter to New York Yankees fans during the Cablevision dispute, YES network president Leo Hindery highlighted his partnership with DirecTV. The letter ran in numerous New York metropolitan area newspapers on March 7, 2002 and encouraged Cablevision subscribers to call 1-800-DirecTV to subscribe. See Richard Sandomir, *Pressure Increases on Cablevision to Carry YES*, N.Y. Times, March 8, 2002, at D1 (discussing open letter).

<sup>33</sup> Richard Sandomir, *YES-Cablevision War Has a Winner: DirecTV*, The New York Times, April 25, 2002 at D2.

<sup>34</sup> Staci D. Kramer, *It's Spring, and Hope Again Springs Eternal*, Cable World, March 17, 2003, at 11.

substantial. Because MVPDs will know these alternatives are available, News Corp. will dramatically increase its ability to raise prices for its programming in negotiations with them.

**A. The Merger Will Increase News Corp.'s Bargaining Power with Rival MVPDs**

News Corp will be able to charge higher prices because the merger will increase its bargaining power with MVPDs. News Corp.'s essential threat when bargaining for higher prices with an MPVD is the threat of withholding programming from the MVPD. This threat will be less costly to News Corp. (and, therefore, more credible) after the merger, because the cost of lost subscription and advertising revenues from withholding programming will be to some extent offset by the increased profits that DirecTV will earn when the rival MVPD is denied this programming. Standard bargaining models in economics all predict that a firm should be able to negotiate higher prices if the option of not selling becomes more attractive to the firm.<sup>35</sup> There are a number of papers in the economics literature that examine the effects of vertical relationships by focusing on how vertical relationships change firms' threat points in bargaining over price.<sup>36</sup>

Of course News Corp.'s threat to withdraw programming will be most credible against small and medium sized cable systems in less dense regions of the country where the withdrawal of programming is more likely to induce its rivals to exit. There are many regions of the country served by small cable systems that have not yet invested in digitalizing their networks. Many

<sup>35</sup> See, e.g., John C. Harsanyi, *Bargaining in The New Palgrave Game Theory*, W.W. Norton (1989); Alvin Roth, *Axiomatic Models of Bargaining*, Springer-Verlag (1979).

<sup>36</sup> See, e.g., Janusz A. Ordover, Garth Saloner, and Steven C. Salop, *Equilibrium Vertical Foreclosure*, 80 *American Economic Review* (1990); Oliver Hart and Jean Tirole, *Vertical Integration and Market Foreclosure*, *Brookings Papers on Economic Activity: Microeconomics 1990* (1990); and Ilya R. Segal and Michael C. Whinston, *Exclusive Contracts and Protection of Investments*, 31 *Rand Journal of Economics* (2000).

analysts have speculated that there is already a danger that many of these firms will simply decide to exit the industry instead of investing more money<sup>37</sup> and the probability of this occurring will only increase to the extent that News Corp. raises their programming prices. If a rival will exit the industry in response to News Corp.'s withdrawal of programming, News Corp. might expect to lose very little programming revenue so long as News Corp. continued to sell its programming to both of the DBS providers because customers of the failed cable system switched to one of them. Therefore even relatively small increases in the profits of DirecTV would be enough to offset these negligible losses or programming revenue. However, this effect would still exist in reduced magnitude even in regions of the country where News Corp could not necessarily expect somewhat to drive a rival MVPD out of business by withholding programming.<sup>38</sup> Furthermore, as will now be explained, the threat to temporarily withdraw programming may provide an even more credible threat in many cases.

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<sup>37</sup> See generally Monica Hogan, *Pity Cable's Rural Ranks*, Multichannel News, June 4, 2001, at 36.

<sup>38</sup> As the owner of 34% of DirecTV, News Corp. is of course automatically entitled to 34% of any increase in profits that DirecTV receives and I believe that in many cases this will be sufficient to significantly increase the credibility of News Corp.'s threat to withhold programming. In particular, so long as News Corp. expects to drive its rival out of business so that the loss of programming revenues will negligible, even a 34% share of the profits will almost surely be significant compared to the negligible revenue loss.

Furthermore, it seems likely to me that News Corp. may well receive more than 34% of the incremental profits it creates for DirecTV by withholding programming from DirecTV's rivals. DirecTV will have its own private incentives to encourage News Corp. to withhold programming from rival MVPDs and is likely to offer News Corp. extra incentives to encourage it to bargain harder and increase the chance that programming will be withheld. (Or, depending upon one's view of the extent to which News Corp. will control DirecTV, it may be that News Corp. will simply demand extra compensation.) For example, DirecTV might agree to accept slightly higher programming prices to the extent that programming is withheld from its rivals. Although an explicit agreement would likely be illegal, informal coordination to achieve this effect should be possible under the umbrella of News Corp.'s joint ownership of both companies. Therefore News Corp. may well receive more than 34% of incremental profits it creates by withholding

**B. Temporary Withdrawal of Programming During Price Disputes Will Be a Particularly Attractive and Credible Threat for News Corp.**

It is important to note that the power of News Corp.'s threat to withdraw programming is magnified immensely by the fact that News Corp. is able to withdraw programming temporarily during disputes over prices. These temporary withdrawals have a minuscule effect on News Corp.'s revenues because the loss of subscription and advertising revenues is only temporary, but they can have a potentially enormous and lasting effect on the MVPD because customers switch to rivals and it is unlikely that they will switch back the instant the programming is restored. As I described in the previous section of this paper, News Corp. can and does routinely withdraw programming as a negotiating tactic when an MVPD will not agree to the terms it asks for.<sup>39</sup> After the merger this imbalance of bargaining power will become even more severe because the lasting losses to the rival MVPD resulting from the fact that customers shift to DirecTV will become lasting gains for News Corp. as the owner of DirecTV.

In fact, it seems likely to me that, once it owns DirecTV, News Corp. may well determine that it is a profitable strategy to begin to more routinely engage in temporary withdrawals of programming from rivals.

As will be seen below in section III(C), most industry participants and industry analysts seem fairly certain that the merger will increase News Corp.'s bargaining power with respect to rival MVPDs.

Finally, the Commission should take into account the extent that News Corp. will be able to increase its ownership share after the merger is approved with no scrutiny or reduced scrutiny. If, for example, News Corp. would be able to increase its ownership level to 100% with very little further scrutiny from the Commission, then it would be appropriate for the Commission to evaluate the harms of the merger at the 100% ownership level now at the last time that the merger will be subject to detailed scrutiny.

<sup>39</sup> I understand that certain rules may make it more difficult for News Corp. to overtly engage in such a strategy for the express purpose of harming an MVPD, but there could be any number of justifications given by News Corp. to comply with the rules while engaging in this gamesmanship.

programming when negotiating agreements with rival MVPDs, even ignoring its effect on News Corp.'s ability to negotiate higher prices. After all, the effect of a short term withdrawal of programming on News Corp.'s programming revenues would be minuscule but, as the owner of DirecTV, there would be a lasting and potentially significant increase in its profits to the extent that customers switch from the rival MVPD to DirecTV. Therefore, it may well be that, after the merger, News Corp. will be "looking for a fight," in the sense that it will actually be able to increase its profits by manufacturing a dispute that would create the pretext for a temporary withdrawal of service. This of course will simply create additional harms for the customers who are affected by these disruptions as well as further magnifying News Corp.'s bargaining power.

**C. There is Widespread Agreement Among Industry Participants and Analysts That The Merger Will Increase News Corp.'s Bargaining Power**

Finally, I find it significant that it is a widely shared belief among industry participants and analysts that the merger will increase News Corp.'s bargaining power. Almost every news story or analyst's report covering this merger mentions this as a significant effect of the merger. Immediately after the merger was announced, the New York Times reported in an article entitled *Murdoch Gets Upper Hand on Cable With Hughes Deal* that:

with the agreement yesterday to acquire the satellite broadcaster DirecTV, Mr. Murdoch, chairman of the News Corporation, can transmit his own channels into homes across the country, redoubling the company's bargaining power with cable operators, television networks, and Hollywood studios.<sup>40</sup>

The same article quoted Robert Kaimowitz, chief executive of the investment fund Bull Path Capital Management as stating that:

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<sup>40</sup> David D. Kilpatrick, *Murdoch Gets Upper Hand on Cable With Hughes Deal*, New York Times, April 10, 2003, at C1.

My sense is that the major purpose for News Corporation controlling DirecTV is to use it as a tactical weapon against the cable companies to get them to pay up for its proprietary programming.<sup>41</sup>

The communications newsletter *Mermigas on Media* further reported that the merger gives News Corp. “unprecedented negotiating leverage with cable operators”<sup>42</sup> and quoted Tom Wolzien, a Sanford Bernstein analyst as stating that News Corp. will obtain through the merger:

four-way leverage against cable operators, competing with satellite and using the requirement that cable get retransmission consent to carry Fox-owned TV stations, while potentially leveraging price for Fox-owned regional sports networks and its national cable and broadcast networks. The threat to cable is that News Corp. might legally withhold programming in a rate dispute in favor of telecasting it exclusively on satellite. At best, this will result in higher program costs to cable operators and shift viewers to satellite.<sup>43</sup>

Kagan sports analyst John Mansell is quoted in another industry publication as stating:

There certainly would be some incremental leverage News Corp. would have over cable operators in terms of regional sports-network rights fees. There’s greater chance of YES-type situations – only it’ll be Fox [networks], and they’ll be even more inclined to go out and promote DirecTV in regions where the cable operator doesn’t pay up.<sup>44</sup>

The impressions of these marketplace observers helps to confirm my view that the transaction would increase News Corp.’s ability to raise programming prices.

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<sup>41</sup> David D. Kilpatrick, *Murdoch Gets Upper Hand on Cable With Hughes Deal*, New York Times, April 10, 2003, at C1.

<sup>42</sup> *Mermigas on Media*, April 16, 2003.

<sup>43</sup> *Id.*

<sup>44</sup> *No Death Star: Cable Takes News-DirecTV Deal in Stride*, Multichannel News, April 14, 2003, at 1 (quoting cable programming executive saying that Murdoch will “use every ounce of his leverage to beat up cable operators who don’t carry his content”).



**IV. THE MERGER WILL INCREASE NEWS CORP.'S INCENTIVE TO RAISE PROGRAMMING PRICES TO RIVAL MVPDS IN ORDER TO DISADVANTAGE THEM**

There is a large body of economics and anti-trust literature that explains why a vertically integrated supplier will generally have an incentive to “raise rivals’ costs” either by raising the price of the inputs it sells rivals or withdrawing them altogether.<sup>45</sup> The idea is that a vertically integrated firm cares about maximizing the joint profits of its upstream and downstream division and that it can generally increase the profits of its downstream division by raising input prices to its rivals. Therefore, there is an extra benefit to raising price and a vertically integrated firm would rationally respond to this extra benefit by raising price higher than it otherwise would. To put this another way, the price that News Corp would charge rival MVPDs to maximize the joint profits of News Corp and DirecTV is larger than the price that News Corp. would charge to maximize the profits of News Corp. alone.<sup>46</sup> It follows that, after the merger, News Corp. will

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<sup>45</sup> See, e.g., Michael H. Riordan & Steven C. Salop, *Evaluating Vertical mergers: A Post-Chicago Approach*, 63 Antitrust L.J. 513 (1995) (overview of vertical mergers); Jonathan B. Baker, *Vertical Restraints Among Hospitals, Physicians and Health Insurers That Raise Rivals’ Costs*, 14 Am. J. L. and Med. 147 (1988) (discussing history of raising rivals’ costs theory); Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals’ Costs to Achieve Power Over Price*, 96 Yale L.J. 209 (1986) (discussing vertical harm in terms of raising rivals’ costs); Steven C. Salop & David T. Scheffman, *Raising Rivals’ Costs*, 73 Am. Econ. Rev. 267, 268 (1983) (discussing exclusionary practices having the effect of raising rivals’ costs).

<sup>46</sup> The profit maximizing price is not infinite because MVPDs pass through price increases to consumers and consumers reduce their demand in response. Therefore one negative consequence to News Corp. of raising the price that it charges to an MPVD is that the MPVD will pass through some if not all of these costs to its customers in the form of higher prices. To the extent that customers of the MPVD discontinue their service because of the price increases, News Corp. will lose both subscription revenue (since the MPVD pays News Corp. on a per subscriber basis) and advertising revenue (since News Corp. will be unable to sell its advertising as much if the subscribership to its programming falls). After the merger this cost of raising prices will be offset by a new benefit. Namely, it is likely that some of the consumers that leave

want to charge a higher price to rival MVPDs for its programming.<sup>47</sup> The incentive to raise rivals' costs will of course be particularly high for the case of small to medium sized cable MSOs in less dense regions of the country since, in these cases, News Corp. might actually be able to completely drive its rival out of business by following such a strategy.

In its recent order extending the exclusive contract prohibition of the program access rules, the Commission reaffirmed its long-standing conclusion that programmers that are vertically integrated with cable systems have the incentive to withhold programming from rival MVPDs in order to increase their own downstream profits.<sup>48</sup> It also noted that the incentive to raise rivals' costs would be particularly great in circumstances where such actions might drive a rival out of business.<sup>49</sup> The same reasoning applies to the case of a programmer that is vertically integrated with a DBS provider. News Corp.'s power over "must have" programming (both

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the MVPD when it passes through price increases will switch to DirecTV and, as an owner of DirecTV, News Corp. will now earn positive profits on each of these consumers.

<sup>47</sup> The fact that News Corp. is acquiring a 34 percent ownership interest in DirecTV instead of a 100 percent ownership should not significantly affect the extent to which News Corp. has the incentive to raise rivals' costs. The overlapping ownership between News Corp. and DirecTV should be more than sufficient to enable them to reach agreements to undertake any actions which maximize their joint profits, so we should expect News Corp. to have the incentive to raise rivals costs to the extent that this will increase the firms' joint profits, just as if it owned 100 percent of DirecTV. The ownership share might affect how the firms split the gains from maximizing their joint profits but it would not affect their incentive to maximize their joint profits. Note that the 34 percent ownership issue has a slightly different effect on the "increasing bargaining power" theory than the "raising rivals' costs" theory. See note 39 for a discussion of the effects of this issue on the "increasing bargaining power" theory.

<sup>48</sup> *Sunset Extension Order*, 17 FCC Rcd at 12147 ¶ 53.

<sup>49</sup> "Moreover, if the long-term result is to limit or eliminate competition, the exclusive arrangement will result in increased profit through the subscribers that migrate from failing or defunct competitors to the programmer's cable affiliate, and through the ability to raise rates without fear of losing subscribers to competitive MVPDs." *Id.*

retransmitted broadcast stations and sports channels) imparts an incentive for it to exert anticompetitive control over these services

#### V. COMPARING THE THEORIES

The theories presented in sections III and IV provide two related but distinct reasons why the merger is likely to result in higher prices. One can think of the bargaining power theory as explaining why News Corp. will have the *ability* to raise prices after the merger and the raising rivals costs theory as explaining why News Corp. will have an increased *incentive* to raise prices after the merger.<sup>50</sup>

The “raising rivals’ costs” theory is generally viewed as the standard explanation for why vertical mergers can cause price increases and is an issue that the Commission has considered and addressed many times before. For example, this was the main issue that motivated Congress to require the Commission to adopt Program Access rules that prohibit programmers who are

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<sup>50</sup> From a slightly more formal economic modeling perspective, the raising rivals’ costs literature typically abstracts away from the bargaining problem completely by simply assuming that the upstream division has all the bargaining power and is able to make a take-it-or-leave-it offer to the rival downstream firm. This literature calculates the profit maximizing take-it-or-leave-it price for the upstream division to offer. The formal result is that the price that maximizes the joint profits of the two divisions is larger than the price that maximizes the upstream division’s profits alone. In bargaining models another price becomes important besides this price. This is the minimum price that the upstream firm would be willing to accept. (This is also the price that the rival downstream firm would offer the upstream division if it had all the bargaining power and could make a take-it-or-leave-it offer to the upstream firm.) Models of bargaining predict that the price the upstream firm is able to negotiate will also generally be affected by the minimum price it would be willing to accept. In terms of this model, the argument in Section III is that the minimum price that the upstream firm is willing to accept goes up once the upstream firm is vertically integrated with the downstream firm. This is because the downstream division’s profits go down when the upstream division makes the input available to the rival downstream firm and the minimum price that the vertically integrated firm will accept must include compensation for the lost profits of the downstream division.

vertically integrated with cable MSOs from discriminating against rivals MVPDs.<sup>51</sup> While this issue is an important concern in this merger and is significant enough in and of itself to warrant the Commission's attention, it is important to note that this merger raises an entirely new and different potential cause for concern, which I do not believe the Commission has ever explicitly addressed before. This is the first reason described above, *viz.*, that the merger will increase News Corp.'s bargaining power and hence its ability to raise prices. Therefore the Commission should be aware that there is potentially an extra cause for concern with this vertical relationship than with many other vertical relationships it has considered before.

#### **VI. CONSUMERS WILL BE HARMED BY THE MERGER**

When News Corp. raises the prices it charges rival MVPDs for programming, consumers will be harmed in the short run because most, if not all, of these programming price increases will be passed through to consumers in the form of increased cable subscription prices. Cable programming networks charge cable systems for their programming on a per subscriber per month basis.<sup>52</sup> Therefore, the cable system views the per month per subscriber fee as a marginal cost of providing service to a customer. It is of course standard economic theory that a firm facing a downward sloping demand curve (as cable systems surely do) will respond to an increase in its marginal costs by increasing price.<sup>53</sup>

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<sup>51</sup> See *Sunset Extension Order* for a recent articulation of this rationale by the Commission.

<sup>52</sup> See *Reply Comments of MediaCom Communications Corporation* for a general discussion of pricing practices for cable network programming.

<sup>53</sup> The FTC concluded that increases in programming prices would result in increases in prices charged to subscribers in its analysis of the TimeWarner Turner Merger. See Federal Trade Commission, *Analysis of Proposed Consent Order to Aid Public Comment*, Federal Register, Vol. 61, No. 187, September 25, 1996, at 50309: "The complaint alleges . . . that substantial increases in wholesale programming costs for both cable systems and alternative service providers – including direct broadcast satellite service and other forms of non-cable distribution

In the long run, the potential harm to consumers will be even greater to the extent that rival MVPDs are either driven out of business or at least weakened to the point where competition is reduced. A reduction in competition would of course cause further price rises for all consumers. The danger of this occurring is especially high in less dense regions of the country where the business case for multiple MVPDs is weakest. In particular, there are many regions of the country served by small cable systems that have not yet invested in digitalizing their networks. Many analysts have speculated that there is already a danger that many of these firms will simply decide to exit the industry instead of investing more money<sup>54</sup> and the probability of this occurring will only increase to the extent that News Corp. raises their programming prices.

**VII. THE CONDITION SUGGESTED BY NEWS CORP IS INADEQUATE TO ADDRESS THE FOREGOING HARMS**

As part of its application for merger approval, News Corp. has offered to abide by the same non-discrimination rules that apply to cable network programmers that are vertically integrated with cable systems. I have a number of serious reservations regarding the adequacy of this proposed condition to address the harms I identify.

**A. The Proposed Condition Does Not Apply to Prices for Retransmission Consent**

News Corp.'s offer to abide by nondiscrimination conditions applies only to the prices it charges for cable network programming and not to the prices it charges for retransmission consent for local broadcast signals. Therefore it leaves a major aspect of the problem

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– would lead to higher service prices and fewer entertainment and information sources for consumers.”

<sup>54</sup> See generally Monica Hogan, *Pagon: Pity Cable's Rural Ranks*, *Multichannel News*, June 4, 2001, at 36.

completely unaddressed. Given that the underlying economic factors are almost exactly the same for the cases of cable network programming and local broadcast signals, there is no reason to treat these two types of programming differently.

**B. The Proposed Condition Allows Quantity Discounts**

Since the proposed condition allows quantity discounts, it places very little constraint on the prices that News Corp. could charge smaller cable systems. DirecTV is certainly much larger than even medium sized cable systems. Therefore News Corp. could always argue that higher prices to these cable systems were justified because it was simply giving a “quantity discount” to DirecTV. As argued above, small and medium sized cable systems are precisely the set of MVPDs for which News Corp. will have the greatest incentive and ability to increase programming prices. Therefore the condition will be most ineffective precisely in the cases where it is needed most.

**C. The Condition Will Be of Limited Effectiveness Because (i) News Corp. Can Raise Prices to All MVPDs Including DirecTV and (ii) There Will be No Out-Of-Region MVPDs Whose Prices Can be Used as a Benchmark**

Finally, even if the above two problems could be solved, the proposed condition only requires that News Corp. charge the *same* prices to all MVPDs. In particular News Corp. could comply fully with the condition and still charge high prices to its rivals simply by charging equally high prices to *all* MVPDs including DirecTV.

Of course, because News Corp. will only own 34 percent of DirecTV after the proposed merger, the public shareholders of DirecTV would be harmed if News Corp. raised prices to DirecTV and one might therefore expect public shareholders or those charged to represent their interests (such as the Audit Committee of the Board of Directors) to stand in the way of such

price increases. For two different reasons, I believe that this factor will not provide any significant restraint on News Corp.

First, when the audit committee examines the program prices that News Corp. charges DirecTV to see if they are “fair,” the only simple objective test it will be able to employ is to examine whether or not DirecTV is being charged more than other MVPDs for the same programs. Since News Corp. only needs to charge DirecTV prices that are as high as those it charges other firms to meet the nondiscrimination condition, it will of course pass this “test” with flying colors. The issue of whether News Corp.’s prices appear to be “too high” relative to other programmers’ prices is an inherently subjective and qualitative issue that an audit committee would find very difficult to make any objectively verifiable determinations about.

Second, even if the Board of Directors of DirecTV had perfect information about all the business decisions of DirecTV and was able to perfectly and fairly represent the interests of the public shareholders, it would still be optimal for them to allow News Corp. to charge high prices to DirecTV so long as News Corp. could find a way to return some of the gains to DirecTV in some other form. This is because DirecTV and News Corp. can maximize their joint profits by doing this (so News Corp. is able to charge high prices to rivals without violating the nondiscrimination condition). News Corp. will be engaging in a broad range of cooperative and joint activities with DirecTV which involve large exchanges of benefits and payments in both directions. In fact, News Corp. touts many of these activities as “efficiencies” related to its ownership of DirecTV. News Corp. could essentially refund some of the high price that it charges DirecTV simply by being slightly more generous in some other exchange.

There is some evidence to suggest that News Corp. has followed precisely this “raise prices to everyone” strategy in the United Kingdom in order to raise prices to rival MVPDs without violating nondiscrimination rules. In the U.K., News Corp. owns a 35 percent interest in British Sky Broadcasting (“BSkyB”) and competes with two cable systems, Telewest and NTL. In addition to its delivery platform, BSKyB has a dominant position in programming in the U.K. The two main providers of cable television in the U.K., Telewest (1.7 million subscribers) and NTL (1.2 million subscribers), have each lost dramatic amounts of money and market share competing with BSKyB,<sup>55</sup> and rising programming costs have been identified as a key culprit.<sup>56</sup> In a recent article in *Fortune* on the proposed News Corp. merger, *Fortune* reported the following conversation with an unnamed cable operator:

‘Look at the U. K. experience,’ says one U.S. cable operator, who’s not ready to speak publicly yet. ‘BskyB, which was controlled by News Corp., had very tight control over movies and sports, and the cost of programming to cable operators was higher than anywhere else in the world.’ Told that Murdoch promises to sell his content to cable and satellite on the same terms, the cable guy replies, ‘It’s easy to overprice programming when you’re paying yourself.’<sup>57</sup>

In addition to the foregoing, it is interesting to note that the failure of the proposed condition to prevent the “charge high prices to everyone” strategy is caused to some extent by the fact that DirecTV has a national footprint. If News Corp. were to merge with an MPVD with

<sup>55</sup> See *Tony Ball*, *Financial Times*, October 29, 2002, at 10 (“during the past year, the shortcomings of ITV Digital, the digital terrestrial platform that collapsed into bankruptcy this year, and the crippling debt burdens of cable groups Telewest and NTL have served only to exaggerate BSKyB’s strength”).

<sup>56</sup> See *Price*, *Telewest Attacks BSKyB Price Rise*, *Financial Times*, January 23, 1998, at 20 (“Telewest Communications, the UK’s second biggest cable company, yesterday blamed price increases by BSKyB, its main supplier of television programmes, for a rise in the number of customers failing to renew their subscriptions last year”).

<sup>57</sup> Marc Gunther, *Murdoch’s Prime Time*, *Fortune*, February 3, 2003.



a less-than-national footprint, then News Corp. would have an incentive to charge lower prices in its out-of-region areas. In this case, the non-discrimination condition would impose a real constraint on New Corp. In order to charge a high price to in-region rivals and maximize its in-region profits, it would also have to charge an equally high price to out-of-region MVPDs which would reduce its out-of-region profits. Therefore, to the extent that News Corp. merged with an MVPD that had a less-than-national footprint, a non-discrimination condition might provide it with some incentive to keep programming prices lower.

The “problem” with the News Corp.-DirecTV case is of course that DirecTV has a national footprint so there will be no out-of-region MVPDs that News Corp. will want to charge low prices to. Therefore, it can charge as high a price as it wishes to its rivals simply by charging an equally high price to DirecTV.

#### **VIII. POTENTIAL CONDITIONS TO REMEDY THE HARMS**

Although the main focus of my paper in this early stage of the proceedings is simply to identify the potential harms of the merger, I will briefly discuss some possible approaches to crafting conditions that might help remedy these harms.

##### **A. Non-Discrimination in Retransmission Consent Pricing**

The most obvious and natural condition to consider is of course that News Corp. extend the same non-discrimination guarantees regarding the prices and terms it offers for its cable network programming to apply also to the prices and terms it offers for retransmission consent of its local broadcast stations. From the perspective of economic fundamentals there is very little difference between these two cases. In both cases, News Corp. is an upstream provider of an important programming input that it sells both to DirecTV and MVPDs that compete with

DirecTV. In my mind there is no economic reason for the Commission to treat these two situations differently. If the Commission determines that the non-discrimination condition is useful and necessary for the upstream product of cable networks then it seems to me that the Commission should be able to apply exactly the same reasoning to conclude that the same condition is useful and necessary for the upstream product of local broadcast signals.

The fact that the existing non-discrimination rules apply to cable network programmers that are vertically integrated with cable systems but do not apply to local broadcast stations that are vertically integrated with cable systems is easy to explain. This is simply because it has been, until very recently, illegal for a company to own a local broadcast station and cable system in the same region, so there has been no need to have a non-discrimination condition for local broadcast stations vertically integrated with cable systems.<sup>58</sup> Now that it has become legal for local broadcast stations to vertically integrate with cable systems that serve the same region, consistency on the part of the Commission will require it to extend its non-discrimination rules to local broadcast stations that are vertically integrated with cable systems. Of course the other fairly recent development in the MVPD market is that DBS is now a significant enough competitor that consistency also requires that the non-discrimination rules should also be generally applied to DBS firms in the same way they are applied to cable systems.

From this perspective, then, in order to be consistent, the Commission should require News Corp. to agree to non-discrimination conditions on both cable network programming and retransmission consent of local broadcast signals. This would deal with the immediate case that has arisen. Then, to make its rules consistent, the Commission should extend its non-

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<sup>58</sup> See 47 U.S.C. § 613 (a)(1) (repealed); 47 C.F.R. § 76.501(a) (vacated).

discrimination rules to apply more generally to any cable network programmer or local broadcast station that is vertically integrated with any MVPD (where in the case of a local broadcast station, the local broadcast station and MVPD serve the same overlapping areas.)

**B. Prohibitions Against Bundling**

A less obvious but still potentially worthwhile approach might be to consider limiting News Corp.'s ability to bundle certain "must have" programming such as its RSNs and retransmission consent for its local broadcast stations together with other programming. It is a widespread and pervasive practice in the industry for network programmers to require MVPDs that want to purchase their "must have" programming to also purchase less desirable programming. News Corp. has been particularly aggressive in bundling its more popular programming, including its local channels, with other less popular or startup channels.<sup>59</sup> However, it is by no means alone in this respect.<sup>60</sup> Therefore network programmers generally find it optimal to exercise whatever market power they have over their "must have" programming both by charging higher prices and by bundling their "must have" programming together with less desirable programming.

From this perspective, one approach to counteracting the increase in market power over "must have" programming that this merger will convey to News Corp. might be to limit the extent it can be exercised by restricting News Corp.'s ability to bundle. The FTC, for example,

<sup>59</sup> A description of these practices is set forth in the comments to which this analysis is attached.

<sup>60</sup> See, e.g., Linda Moss & Mike Farrell, *Viacom Buys Custody: Comedy Central Joins MTVN Stable*, Multichannel News, April 28, 2003, at 1 ("MTVN has a history of buying networks and bundling them with MTV or Nickelodeon, raising the service's rates in the process..."); Linda Moss, *Primer on Dropping Nets Could Draw Lots of Ops*, Multichannel News, October 14, 2002, at 1 (describing small cable operators' efforts to evade programmer bundling and other requirements).

followed this approach in the conditions it placed on the Time Warner Turner merger by prohibiting the merged firm from engaging in certain types of bundling.<sup>61</sup>

#### CONCLUSION

The proposed merger between News Corp. and DirecTV will give News Corp. both the incentive and ability to charge higher programming prices to MVPDs that are rivals of DirecTV. In the short run this will harm consumers because these price increases will be passed through to them in the form of higher subscription prices. In the long run, price increases to MVPDs will harm competition at the MVPD level -- especially in less dense regions of the country where the business case for multiple MVPDs is more tenuous -- as DirecTV's rivals will be driven out of business or fundamentally weakened. In those markets, DirecTV will eventually be able to increase prices even more. The non-discrimination condition proposed by News Corp. does not apply to retransmission consent and is weakened by allowing quantity discounts. More fundamentally, the condition imposes a limited constraint on News Corp. even if these problems could be solved because News Corp. can simply respond by charging high programming prices to all MVPDs including DirecTV.

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<sup>61</sup> See Decision and Order, *In the Matter of Time Warner Inc., a corporation; Turner Broadcasting System, Inc., a corporation*, 123 F.T.C. 171 at Section V (February 3, 1997) ("*Time Warner/Turner*") (prohibiting the merged entity from bundling each firm's most popular networks with other, less popular networks).

I declare that the foregoing is true and correct:

  
William P. Rogerson

Dated:

June 13, 2003

**EXHIBIT 1****Curriculum Vitae of William P. Rogerson****Personal**

Date of birth: November 7, 1955  
Citizenship: American

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**Education**

B.A., Economics, University of Alberta, 1976  
Ph.D., California Institute of Technology, 1980

**Current Employment**

Professor of Economics, Northwestern University

**Honors, Awards and Research Grants**

Graduated from the University of Alberta with distinction, 1976  
Earl C. Anthony Fellowship, 1976-77  
Canada Council Doctoral Fellowship, 1979-80  
Shelby Cullom Davis Fellowship, 1979  
NSF Grant SES-8320451, "Moral Hazard, Reputation, and Product Quality,"  
March 1984 - March 1985  
NSF Grant SES-8504304, "Moral Hazard, Reputation, and Product Quality."  
April 1985 - September 1987  
NSF Grant IRI-8705477, "Contracting Under Asymmetric Information,"  
July 1987 - December 1989  
Named to Household International Professorship in Economics, September  
1987 - August 1989  
Lynde & Harry Bradley Foundation Research Grant, "An Economic Analysis  
of Defense Procurement Regulations," June 1989 - December 1991.  
NSF Grant SES-8906751, "Profit Regulation of Defense Contractors," August  
1, 1989 - July 31, 1991.  
Olin Fellow at The Center for the Study of the Economy and the State,  
University of Chicago, October 1, 1989 - June 30, 1990.  
Smith Richardson Foundation, Inc. Research Grant, "Economic Incentives and the Defense  
Procurement Process," March 1, 1993 - May 31, 1995.  
Elected a Fellow of the Econometric Society, 1999.

**Research and Teaching Interests**

Industrial Organization, Regulation, Telecommunications, Cost Accounting, Defense Procurement, and Health Care.

**Employment History**

Research Assistant to Canadian Member of Parliament, Arnold Malone,  
June 1975 - September 1975  
Teaching Assistant at University of Alberta, September 1975 - June 1976  
Economist, Department of Industry, Trade and Commerce, Government of Alberta, June 1976 - September 1976  
Research Assistant, Environmental Quality Laboratory, Caltech,  
June 1977 - September 1977  
Economist, Long Range Planning and Structural Analysis Division, Department of Finance, Government of Canada, June 1978 - September 1978  
Teaching Assistant to Professor Charles R. Plott, Division of Humanities and Social Sciences, Caltech, September 1979 - June 1980  
Assistant Professor of Economics, Stanford University, September 1980 - August 1984  
Associate Professor of Economics, Northwestern University, September 1984 - May 1990  
Professor of Economics, Northwestern University, May 1990 - Present  
Chair, Economics Department, Northwestern University, September 1996 - August 1998.  
Chief Economist, Federal Communications Commission, June 1, 1998-May 31, 1999 (on leave from Northwestern for this year.)  
Director, Northwestern Program in Mathematical Methods in the Social Sciences, September 2000- present.

**Professional Activities**

Editor of Defense and Peace Economics, January 1995 - December 1998.  
Member of the editorial board of Defense and Peace Economics, September 1991 - December 1998.  
Member of the editorial board of Review of Accounting Studies,  
September 1993 to present.  
Member of the editorial board of Journal of Industrial Economics, October 1995- Sept. 1998.  
Chief Economist of Federal Communications Commission, June 1, 1998 - May 31, 1999.  
Member of the Illinois Economic Policy Council, September 1999 to September 2000  
Consultant to: Federal Communications Commission, Federal Trade Commission, Institute for Defense Analysis, Logistics Management Institute, Office of the Secretary of Defense (Program Analysis and Evaluation), RAND Corporation, US Department of Justice

**Refereed Publications**

"Aggregate Expected Consumer Surplus As a Welfare With an Application to Price Stabilization," *Econometrica*, 49, No. 2, (March 1980), pp. 423-436.  
"Agriculture in Development: A Game-Theoretic Analysis," with Robert Bates, *Public Choice*, 35, (1980), pp. 513-527.  
"The Social Costs of Monopoly and Regulation: A Game-Theoretic Analysis," *Bell Journal of Economics*, 13, No. 2, (Autumn 1982), pp. 391-401.  
"Reputation and Product Quality," *Bell Journal of Economics*, 14, No. 2, (Fall 1983), 508-515.



- "Consumer Misperceptions, Market Power and Product Safety," with Mitchell Polinsky, *Bell Journal of Economics*, 14, No. 2, (Fall 1983), 581-589.
- "A Note on the Incentive for a Monopolist to Increase Fixed Costs as a Barrier to Entry," *Quarterly Journal of Economics*, 396, May 1984, 399-402.
- "Efficient Reliance and Damage Measures for Breach of Contract," *Rand Journal of Economics*, Spring 1984, 39-53.
- "Repeated Moral Hazard," *Econometrica*, 53, January 1985, 69-76.
- "The First-Order Approach to Principal Agent Problems," *Econometrica*, 53, November 1985, 1357-1368.
- "Robust Trading Mechanisms" with Kathleen Hagerty, *Journal of Economic Theory*, 42, June 1987, 94-107.
- "The Dissipation of Profits by Brand Name Capital and Entry When Price Guarantees Quality," *Journal of Political Economy*, 95, August 1987, 797-809.
- "A Note on the Existence of Single Price Equilibrium Price Distributions," *Review of Economic Studies*, 54, April 1987, 339-342.
- "Price Advertising and the Deterioration of Product Quality," *Review of Economic Studies*, 55, April 1988, 215-230.
- "Profit Regulation of Defense Contractors and Prizes for Innovation," *Journal of Political Economy*, 97, December 1989, 1284-1305.
- "Quality vs. Quantity In Military Procurement," *American Economic Review*, 80, March 1990, 83-92.
- "Excess Capacity in Weapons Production: An Empirical Analysis," *Defence Economics*, 2, 1991, 235-250.
- "Optimal Depreciation Schedules for Regulated Utilities," *Journal of Regulatory Economics*, 4, 1992, 5-33.
- "Contractual Solutions to the Hold-Up Problem," *Review of Economic Studies*, 59, October 1991, 777-794.
- "Incentives, the Budgetary Process, and Inefficiently Low Production Rates in Defense Procurement," *Defence Economics*, 3, 1991, 1-18.
- "Overhead Allocation and Incentives for Cost Minimization in Defense Procurement," *The Accounting Review*, 67, 1992, 671-690.
- "Choice of Treatment Intensities by a Nonprofit Hospital Under Prospective Pricing," *Journal of Economics and Management Strategy*, 3(1), Spring 1994, 7-52..
- "Economic Incentives and the Defense Procurement Process," *Journal of Economic Perspectives*, 8(4), Fall 1994, 65-90.
- "Inter-Temporal Cost Allocation and Managerial Investment Incentives," *Journal of Political Economy*, 105(4), 1997, 770-795.
- "The Regulation of Broadband Telecommunications, The Principle of Regulating Narrowly Defined Input Bottlenecks, and Incentives for Investment and Innovation," *University of Chicago Legal Forum*, 2000, 119-147.
- "The Use of Simple Menus of Contracts in Cost-Based Procurement and Regulation," *American Economic Review*, June 2003, *forthcoming*.

**Other Publications**

- "Electric Generation Plants" Appendix F.1 in *Implementing Tradable Emissions Permits for Sulfur Oxides Emissions in the South Coast Air Basin*, Vol. II, by Glen R. Cass, Robert W. Hahn, Roger G. Noll, ARB Contract No. A8-141-31, June 30, 1982.
- "A Comment on Political Institutions and Fiscal Policy: Evidence from the U.S. Historical Record," *Journal of Law Economics and Organization*, 6, Special Issue, Conference on "The Organization of Political Institutions", 1991, 155-166.
- "Inefficiently Low Production Rates in Defense Procurement: An Economic Analysis," Leitzel, Jim and Jean Tirole, eds., *Incentives in Defense Procurement*. Boulder: Westview Press, 1993.
- Profit Regulation of Defense Contractors and Prizes for Innovation*, RAND, R-3635-PA&E, 1991.
- An Economic Framework for Analyzing DoD Profit Policy*, RAND, R-3860-PA&E, 1991.
- Overhead Allocation and Incentives for Cost Minimization in Defense Procurement*, RAND, R-4013-PA&E, 1992.
- "Review of 'A Theory of Incentives in Procurement and Regulation,'" book review, *Journal of Political Economy*, 102, 1994, 397-402
- On the Use of Transfer Prices in DoD: The Case of Repair and Maintenance of Depot Level Repairables by the Air Force*, Logistics Management Institute Paper PA303RD2, January 1995, Logistics Management Institute, McLean, VA.
- "Incentive Models of the Defense Procurement Process," in Hartley, Kieth, and Todd Sandler, eds., *The Handbook of Defense Economics*, North Holland, 1995, 309-346..
- "The Economics of University Indirect Cost Reimbursement in Federal Research Grants," (with Roger Noll) in Roger Noll, ed., *Challenges to the Research University*. Washington: Brookings Institution, 1997.
- "New Economic Perspectives on Telecommunications Regulation." (review of *Competition in Telecommunications*, by Jean-Jacques Laffont and Jean Tirole), *University of Chicago Law Review*, 67, Fall 2000, 1489-1505.

Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, DC 20554

In the Matter of:	)	
	)	
General Motors Corporation, Hughes	)	
Electronics Corporation, and the	)	
News Corporation Limited Application	)	MB Docket No. 03-124
To Transfer Control of FCC	)	
Authorizations And Licenses Held By	)	
Hughes Electronics Corporation	)	
To The News Corporation Limited	)	

**AFFIDAVIT OF LYNN A. STOUT**

1. My name is Lynn A. Stout. I hold the position of Professor of Law at the University of California at Los Angeles (UCLA) School of Law, where I teach basic and advanced courses in securities regulation and corporate law. I have also taught at the Georgetown University Law Center, George Washington University's National Law Center, Harvard Law School, and the New York University School of Law. A copy of my current *curriculum vitae* is attached.

2. I have been asked by the Joint Cable Commenters to examine the Consolidated Application for Authority to Transfer Control (Application) filed by General Motors Corporation (GM), Hughes Electronics Corporation (Hughes), and The News Corporation Limited (News Corp.) in this proceeding. Specifically, I have been asked to examine the proposed corporate structure of Hughes and to analyze whether the potential for self-dealing transactions between Hughes (including affiliates of Hughes) and News Corp. (including affiliates of News Corp.) can be addressed by a Hughes board

of directors with a majority of “independent” directors and an Audit Committee comprised only of “independent” directors.

3. As described in greater detail below, I conclude that, under Delaware law, the potential for self-dealing transactions between Hughes and News Corp. is not addressed by a Hughes board of directors with a majority of “independent” directors and an Audit Committee comprised only of “independent” directors.” Nor is the problem of controlling shareholder self-dealing addressed by provisions of the Sarbanes-Oxley Act designed to deter officer and director self-dealing (e.g., provisions restricting corporate loans to officers and directors), or by New York Stock Exchange (NYSE) proposed listing requirements for majority-independent boards and independent audit committees.

4. My analysis is based on the facts described in the May 2 Application and its Attachments B, C, D, E, and G, as well as Appendixes C and D (the proposed Hughes Charter and By-laws) filed with the Securities and Exchange Commission on June 5, 2003.

5. These documents describe the proposed governance structure of Hughes as follows. Hughes' present shareholder, GM, will split off Hughes and divest itself of its interest in Hughes. Hughes will become a publicly-traded Delaware corporation. Hughes will continue to own indirectly all interests in DirecTV Enterprises, LLC (DirecTV). (Application at page 4.) News Corp. will acquire, through its subsidiary Fox Entertainment Group, Inc., a 34% interest in Hughes. As a result, News Corp. will become the single largest shareholder of Hughes. Rupert Murdoch, the Chief Executive Officer (CEO) of News Corp., will become the Chairman of the Hughes Board of Directors. (Application at pages 1-2, 10-13.) The Hughes CEO will be Chase Carey, a

former News Corp. co-Chief Operating Officer (COO). (Application at page 13.) Hughes' board will consist of eleven members, six of whom are described in the Application as "independent." (Application at page 13, Attachment D at D-3.) In addition, the board will have an Audit Committee comprised entirely of "independent" directors. (Application at page 13.)

6. The meaning of "independent" is not defined in the Application. However, the proposed Hughes Charter states that the meaning of independent "may be defined from time to time in the By-Laws." (Charter at Article V, Section 5.) The proposed Hughes By-Laws, which can be amended at any time by the Hughes board of directors (Charter at Article VII), define an independent director as a director who qualifies as such under the rules and regulations of the New York Stock Exchange or, if such rules are not in effect, a director who, "as determined in good faith by the Board," has no relationship to Hughes "that may interfere with the exercise of his or her independence from management of [Hughes] and [Hughes] and no material relationship with any member of the Purchaser Group ..." For purposes of this Affidavit, I use that definition.

7. The Application states that any subsequent transactions entered into between Hughes and its controlling shareholder News Corp., such as a programming contract between Hughes' subsidiary DirecTV and a News Corp. programming affiliate, "may be subject to review and approval by the independent Audit Committee." (Application at page 14, emphasis added.) The Application then concludes that this potential for audit committee review will "ensure that such contract is on arm's length terms." (Application at page 59.)

8. This conclusion is incorrect.

**I. UNDER DELAWARE LAW, NEWS CORP. WOULD BE THE DE FACTO CONTROLLING SHAREHOLDER OF HUGHES**

9. As a result of the proposed transactions, News Corp. will become the single largest shareholder of Hughes, with a stake amounting to 34% of Hughes' outstanding shares. The next-largest shareholder, a collection of trusts established under various GM employee benefit plans, will hold only about 20%. The remaining 46% of Hughes shares will be widely held by the public at large. (Application at page 13.)

10. This ownership structure makes a compelling case that News Corp. will be the *de facto* controlling shareholder of Hughes. The case for *de facto* control is further strengthened by the facts that the Hughes CEO will be Chase Carey, a former News Corp. co-COO, that Hughes' board will be Chaired by News Corp.'s present CEO, Rupert Murdoch, and that five members of Hughes' eleven-member board will be "interested" directors.

11. The Application concedes that, in light of these factors, "the Commission may deem News Corp. to exercise *de facto* control over Hughes under its totality of the circumstances test for purposes of the Communication Acts." (Application at page 14.) For similar reasons, News Corp. would likely be deemed the *de facto* controlling shareholder of Hughes for purposes of Delaware corporate law. *Solomon v. Armstrong*, 747 A.2d 1098, 1116 n.53 (Del Ch. 1999).

**II. A TRANSACTION BETWEEN A CONTROLLING SHAREHOLDER AND A PARTIALLY-OWNED SUBSIDIARY IS SELF-DEALING UNLESS THE CONTROLLING SHAREHOLDER CAN PROVE "ENTIRE FAIRNESS"**

12. Delaware law treats any transaction or contract between a controlling parent corporation and its partially-owned subsidiary as an "interested" transaction.

*Sinclair v. Levien*, 280 A.2d 717 (Del. 1971). Such interested transactions are intrinsically suspect, on the straightforward theory that a controlling parent can use its influence over a partially-owned subsidiary (including its influence over the subsidiaries' directors) to pursue deals that extract wealth from the subsidiary in a fashion that benefits the controlling shareholder exclusively, while sharing the harm between the subsidiary's controlling and noncontrolling shareholders.

13. The classic example of this is the case where a parent uses its influence to cause a partially-owned subsidiary to enter a contract requiring the subsidiary to buy or sell goods or services from the parent on terms that are less favorable than those the subsidiary could obtain in arm's length transactions. This is the archetype of "self-dealing," because it allows a controlling shareholder to extract a benefit from the subsidiary firm "to the exclusion of, and detriment to, the minority shareholders of the subsidiary." *Sinclair v. Levien*, 280 A.2d 717, 720 (Del. 1971).

14. Recognizing the unavoidable conflict of interest presented by transactions between a parent and a partially-owned subsidiary, Delaware corporate law treats such transactions as intrinsically suspect and subject to challenge by the subsidiary's noncontrolling shareholders, who can bring suit against the controlling shareholder alleging self-dealing in breach of the shareholder's fiduciary duty of loyalty. The controlling shareholder accused of self-dealing will be found liable unless it can prove that the transaction was entirely "fair" to the subsidiary. "Fairness" requires a demonstration of both "fair dealing" (that is, a fair negotiating process) and a "fair price." *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983).<sup>1</sup>

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<sup>1</sup> The burden of showing entire fairness normally rests on the controlling shareholder. However, in some circumstances, if the interested transaction is approved after full disclosure by the vote of a majority of the

15. Notwithstanding the fact that a noncontrolling shareholder can, in theory, sue a controlling shareholder for self-dealing, in practice there are substantial barriers to doing this. Noncontrolling shareholders cannot be expected to know of self-dealing transactions in advance, nor even always to detect them when they occur. Even if self-dealing is detected, noncontrolling shareholders may lack the resources or inclination to undertake the litigation involved in trying to establish breach of duty. Moreover, it can be extremely difficult to establish damages in cases where controlling parents and partially-owned subsidiaries enter complex agreements, because of the difficulties of establishing what a “fair price” should be.

16. Moreover, transactions between parent and subsidiary corporations often give rise to common economic benefits (through economies of scope, tax offsets, etc.) that are not available in transactions between unrelated corporations. Delaware law does not require a controlling shareholder to share these common benefits with the subsidiary or the subsidiary’s noncontrolling shareholders, because it does not treat a failure to share as a detriment to minority shareholders. *Sinclair v. Levien*, 280 A.2d 717, 720 (Del. 1971); *Getty Oil Co. v. Skelly Oil Co.*, 267 A.2d 883 (Del. 1970).

17. For these reasons, noncontrolling shareholders’ theoretical standing to bring lawsuits challenging self-dealing transactions cannot be expected to deter all such transactions, nor to prevent a controlling shareholder from retaining for itself the benefits from parent-subsidiary transactions.

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firm’s noncontrolling shareholders, the burden of showing unfairness will shift to the noncontrolling shareholders challenging the transaction. *Williams v. Geier*, 671 A. 2d 1368, 1382 (Del. 1996). It should be noted however that such noncontrolling shareholder ratification does *not* immunize a controlling shareholder from liability for self-dealing, but merely shifts the burden to the plaintiff to show unfairness in the transaction. *Solomon v. Armstrong*, 747 A.2d 117, 1116-17 (Del. Ch. 1999).



**III. "INDEPENDENT" DIRECTOR APPROVAL DOES NOT REMEDY A SELF-DEALING TRANSACTION BETWEEN A CONTROLLING SHAREHOLDER AND A SUBSIDIARY**

18. The Application suggests that interested transactions between News Corp. and Hughes "may be subject to review and approval" by an Audit Committee comprised only of Hughes' "independent" directors. (Application at page 14.) The Application then suggests that the potential for review will ensure that any interested transactions occur only on "arm's length terms." (Application at page 59.)

19. These statements do not paint an accurate picture of the legal effect of independent director approval on controlling shareholder liability under Delaware law. The concept of the "independent" director developed in corporate law not to address the problem of controlling shareholder self-dealing, but a different problem: officer and director self-dealing. Directors and officers of a firm may be tempted to extract wealth from the firm through self-interested transactions that harm all the firm's shareholders, controlling and noncontrolling alike. (Lavish executive compensation contracts are an example).

20. A variety of legal rules and doctrines address the problem of director and officer self-dealing, often by encouraging contracts between the firm and officers or directors to be negotiated or approved by "independent" directors who do not themselves have a personal interest in the transaction. Such solutions can be found, *inter alia*, in Section 144 of the Delaware corporate code, which addresses interested transactions between the firm and its directors; in certain provisions of the Sarbanes-Oxley act, for example rules prohibiting loans between the firm and its officers and directors; and in the NYSE's proposed listing requirement of a board with a majority of independent members and an audit committee comprised entirely of independent directors.

21. However, the problem of officer and director self-dealing is not particularly relevant to the proposed acquisition of a controlling block of Hughes by News Corp. As discussed above, the primary problem raised by the proposed acquisition is controlling shareholder self-dealing.

22. As a result the potential for controlling shareholder self-dealing raised by the proposed acquisition is not well addressed by the sorts of solutions offered in Section 144, Sarbanes-Oxley, or the NYSE's proposed listing rules. These solutions were not developed to prevent a controlling stockholder from exerting influence over a partially-owned subsidiary, and do not remedy that problem.

23. Delaware Section 144, Sarbanes-Oxley, and the NYSE's proposed rules for independent directors do not remedy the problem of controlling shareholder self-dealing because, in a very basic sense, no director reliably can be "independent" of a controlling shareholder's influence. Each director owes a fiduciary duty to that shareholder, and each also must recognize that if he goes against the controlling shareholder he will likely lose his position on the board. The result is that even "independent" directors may, as a practical matter, be dominated by and defer to a controlling shareholder. *Kahn v. Lynch Communications Systems*, 638 A.2d 1110, 1115 (Del. 1994). For this reason, Delaware law does not mandate "independent" director review and approval of transactions between a controlling shareholder and the firm: such review and approval cannot suffice to give a clean bill of health to transactions that are by their very nature tainted with conflict of interest. (It is worth noting that the Application only claims that transactions between News Corp. and Hughes "may be subject to review

and approval” by the Audit Committee; this careful phrasing correctly recognizes that nothing in Delaware law requires this).

24. Review and approval of transactions between the firm and a controlling shareholder by a board committee comprised of directors who are not themselves employees of the controlling shareholder can, perhaps, help towards establishing the “fair dealing” prong of the two-prong “entire fairness” test. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 709 n.7 (Del. 1983). However, it is important to note that this arrangement alone does not guarantee a judicial finding of fair dealing, because directors who are nominally “independent” may nevertheless defer to a controlling shareholder. *Kahn v. Lynch Communications Systems*, 638 A.2d 1110, 1115 (Del. 1994). Moreover, a finding of fair dealing does not address the issue of fair price. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983). Finally, even in a case where a controlling shareholder could establish both fair dealing and fair price, the result would not be to immunize the controlling shareholder from liability, but simply to shift the burden to the plaintiff of showing unfairness. *Kahn v. Lynch Communications Systems*, 638 A.2d 1110, 1117 (Del. 1994).

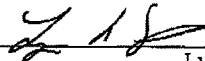
25. The net result is that Delaware law does not mandate that the “independent” directors of a partially-owned subsidiary review and approve self-dealing transactions between the subsidiary and its controlling shareholder. Even if review occurs, it does not insulate such transactions from challenge but only contributes to a showing of the “fair dealing” aspect of the “entireness fairness” Delaware law seeks in such transactions, or, at most, shift the burden to noncontrolling shareholders to establish unfairness. Similarly, neither the Sarbanes-Oxley Act nor the rules of the New York

Stock Exchange remedy the potential for controlling shareholder self-dealing that would arise in connection with transactions between News Corp. and Hughes

**CONCLUSION**

26. For the reasons stated above, I conclude that the proposed acquisition by News Corp. of a controlling block of Hughes would raise problems of controlling shareholder self-dealing that cannot be addressed by a Hughes board with a majority of "independent" directors, nor by the existence of an Audit Committee comprised only of independent directors.

I declare that the foregoing is true and correct:

  
\_\_\_\_\_  
Lynn A. Stout  
Professor of Law

Dated: 5/13/03

**Testimony of Rupert Murdoch  
Chairman and Chief Executive**

**The News Corporation, Ltd.**

**Before the Senate Judiciary Subcommittee on  
Antitrust, Competition Policy, and Consumer Rights**

**“The News Corp/Direct TV Deal: The Marriage of  
Content and Global Distribution”**

**June 18, 2003**

**Testimony of Rupert Murdoch  
Chairman and Chief Executive**

**The News Corporation, Ltd.**

**Before the Senate Judiciary Subcommittee on Antitrust  
Competition Policy, and Consumer Rights**

**“The News Corp/Direct TV Deal: The Marriage of Content and  
Global Distribution”**

**June 18, 2003**

Good afternoon Chairman DeWine, Senator Kohl, and Members of the Subcommittee. Thank you for the invitation to testify today regarding News Corporation's proposed acquisition of a 34% interest in Hughes Electronics Corporation.

Let me say at the outset that we believe that this acquisition has the potential to profoundly change the multichannel video marketplace in the United States to the ultimate benefit of all pay-TV customers, whether they are direct-to-home satellite or cable subscribers. It is my hope, and my goal, that as a result of this acquisition, Hughes' DIRECTV operation will be infused with the strategic vision, expertise, and resources necessary for it to bring innovation and competition to the multichannel marketplace and, of course, to the televisions of tens of millions of American viewers.

The public interest benefits of this transaction are manifold, but I would like to briefly touch on three key areas today:

First, News Corporation's outstanding track record of providing innovative new products and services to consumers, a track record that it is determined to replicate at Hughes and DIRECTV;

Second, the specific consumer benefits that will be realized from this transaction, including improvements in local-into-local service, new and improved interactive services, and the many new diversity programs News Corporation will bring to Hughes; and

Third, the absence of any horizontal or vertical merger concerns about this transaction. This transaction will only increase the already-intense competition in the programming and distribution markets, and market realities will compel our companies to continue the open and non-discriminatory practices each company has lived by. Nonetheless, to eliminate any possible concerns over the competitive effects of vertical integration, the parties have agreed as a matter of contract to significant program access commitments, and have asked the FCC to make those commitments an enforceable condition of the transfer of Hughes' DBS license.

News Corporation's track record of innovation as a content provider and as a satellite broadcaster is without parallel. Our company has a history of challenging the established – and often stagnant – media with new products and services for television viewers around the world. Perhaps our first and best-known effort to offer new choices to consumers in the broadcasting arena came with the establishment of the FOX network in 1986. FOX brought much-needed competition to the "Big 3" broadcast networks at a time when conventional wisdom said it couldn't be done. Seventeen years later, we have proved unambiguously that it could be done, with FOX reigning as the number one network so far this calendar year in the highly valued "adults 18-49" demographic. Along the way, we redefined the TV genre with shows like *The Simpsons*, *In Living Color*, *The X-Files*, and *America's Most Wanted*, and more recently *24*, *Boston Public*, *Malcolm in the Middle*, *The Bernie Mac Show*, and the biggest hit on American TV, *American Idol*.

The FOX network was launched on the back of the Fox Television Stations group, an innovator in local news and informational programming since it was first formed. Today, Fox-owned stations air more than 800 hours of regularly scheduled local news each week – an average of 23 hours per station. We have increased the amount of news on these stations by 57 percent, on average, compared to the previous owners. Viewers demand more local news, and we provide it. Fox-owned stations were often the first – and in many markets are still the only – stations to offer multiple hours of local news and informational programming each weekday morning. This commitment to local news extends well beyond the stations we own. Since 1994, Fox has assisted more than 100 affiliates in launching local newscasts.

In addition to providing greater choice and innovation in network entertainment and local news, we have also redefined the way Americans watch sports. With viewer-friendly innovations such as the "FOX Box" and the first "Surround Sound" stereo in NFL broadcasts, the catcher cam in baseball, the glowing puck in hockey, and the car-tracking graphic in NASCAR, FOX has made sports more accessible and exciting for the average fan. FOX Sports Net, launched in 1996, has provided the first and only competitive challenge to the incumbent sports channel, ESPN. Fox Sports Nets' 19 regional sports channels, reaching 79 million homes, regularly beat ESPN in several key head-to-head battles. In 2002, Major League Baseball on ESPN averaged a 1.1 rating. On Fox Sports Net, baseball scored an average 3.5 rating in the markets it covers. The NBA on ESPN has averaged a 1.2 rating during the current season. In Fox Sports Net's markets, it has rated a 2.2. The key to Fox Sports Net's success is its delivery of what sports fans want most passionately: live, local games, whether at the professional, collegiate, or high school level, coupled with outstanding national sports events and programming.

Perhaps News Corp.'s most stunning success against conventional wisdom—and our most innovative disruption of the status quo—is the Fox News Channel, launched in 1996. A chorus of doubters said CNN *owned* the cable news space and no one could possibly compete. A scant five years later, Fox News Channel overtook CNN, and since early 2002 has consistently finished first among the cable news channels in total day ratings. Growing from 17 million subscribers at launch to almost 82 million subscribers this month, Fox News Channel boasts some of the most popular shows on cable and satellite. I think it is fair to say Fox transformed the cable news business, introducing innovative technology and programming, and bringing a fresh choice and perspective to American news viewers.

Across the dial on American television are examples of where our challenges to the status quo have made a difference for viewers and proven we could be competitive against entrenched competition. We've launched and expanded FX, a general entertainment channel; we've launched the movie channel FXM; and we've re-launched and expanded the Speed Channel, a channel devoted to auto racing enthusiasts. And in January 2001, we launched National Geographic Channel with our partner, the National Geographic Society, into nine million homes. Today, Nat Geo is the fastest-growing cable network in the nation with 43 million subscribers and is making steady progress in the ratings against the established industry leader, The Discovery Channel.



News Corp.'s track record of innovation is not limited to the United States. News Corp. will bring a wealth of innovation to Hughes and DIRECTV from its British DTH platform, BSkyB. We launched BSkyB in 1989 with only four channels of programming. In 1998, frustrated by the limitations of analog technology and determined to give viewers even wider choices, BSkyB launched a digital service that boasted 140 channels. In 1999, in order to speed the conversion to digital and to drive penetration, BSkyB offered free set-top boxes and dishes. The conversion to digital took three years and cost BSkyB nearly one billion dollars, but by 2001, when the transition to digital was complete, BSkyB's subscriber base had grown to 5 million homes. Through BSkyB's digital offering, BSkyB viewers may choose from 389 channels delivering programming 24 hours each day. They also have a vast array of new services, including world-first interactive innovations such as a TV news service that allows viewers to choose from multiple segments being broadcast simultaneously on a news channel, multiple camera angles during sporting events, or multiple screens of programming within a certain genre. In addition, BSkyB viewers have access to online shopping, banking, games, email, travel, tourism and information services. With the launch of Europe's first fully integrated digital video recorder in 2001, BSkyB customers won access to even more interactive capabilities and viewing choices.

Upon completion of this transaction, News Corp. will bring the same spirit of innovation to the DBS business in the U.S, in the process redefining the choices Americans have when they watch television. This spirit of never-say-die competition and News Corp.'s demonstrated determination to provide ever-expanding services to the public have the potential to re-energize the entire American multichannel video marketplace.

To my second point about this transaction: its benefits to consumers. Apart from a history of bringing new competition and innovation to the television industry, News Corp. has been tremendously successful in bringing tangible benefits to consumers over nearly two decades of operating both here in the United States and abroad. This transaction will be no exception, enabling us to share our best practices across our platforms and across geographical boundaries to the benefit of consumers. These benefits will be very real, and often easily quantifiable.

One of the first enhancements to DIRECTV's service that News Corp.'s investment in Hughes will bring will be more local television stations for subscribers, offering consumers a more

compelling alternative to cable. News Corp., as a leading U.S. broadcaster, was the first proponent of local-into-local service as part of our American Sky Broadcasting ("ASkyB") satellite DTH venture six years ago. In fact, I testified before Congress on this very topic, urging passage of copyright legislation to allow the retransmission of local signals by DBS. ASkyB conceived and designed a DBS spot beam satellite to implement this previously unheard of idea. As a broadcast company, News Corp. was convinced then – as it is now - that DBS will be the strongest possible competitor to cable only if it can provide consumers with the local broadcast channels they have come to rely on for local news, weather, traffic and sports.

With that in mind, News Corp. is committed to dramatically increasing DIRECTV's present local-into-local commitment of 100 DMAs by providing local-into-local service in as many of the 210 DMAs as possible, and to do so as soon as economically and technologically feasible. To that end, we are already actively considering a number of alternative technologies, including using some of the Ka-band satellite capacity on Hughes Network Systems' SPACEWAY system; seamlessly incorporating digital signals from local DTV stations into DIRECTV set-top boxes equipped with DTV tuners; and by exploring and developing other emerging technologies that could be used to deliver local signals, either alone or in combination with one of the above alternatives.

In addition, News Corp. is exploring new technologies that promise to improve spectrum efficiency or otherwise increase available capacity so that DIRECTV can expand the amount of HDTV content. Options include use of Ka-band capacity, higher order modulation schemes, such as the 8PSK technology FOX uses for its broadcast distribution to affiliated stations, and further improvements in compression technology. News Corp. will urge DIRECTV to carry many more than the four HDTV channels it currently carries and the five channels that some cable operators carry. In this way, we hope to help drive the transition to digital television by providing compelling programming in a format that will encourage consumers to invest in digital television sets.

As to broadband, News Corp. will work aggressively to build on the services already provided by Hughes to make broadband available throughout the U.S., particularly in rural areas. Broadband solutions for all Americans could come from partnering with other satellite broadband providers, DSL providers, or new potential broadband providers using broadband over power line systems, or from other emerging technologies. News Corp. believes it is critical

that consumers have vibrant broadband choices that compete with cable's video and broadband services on capability, quality and price.

The public will also benefit from the efficiencies and economies of scope and scale that News Corporation will bring to DIRECTV. We believe by sharing "best practices," and by using management and expertise from our worldwide satellite operations, we will be able to substantially reduce DIRECTV's annual expenses by \$65 to \$135 million annually. Other efficiencies include sharing facilities of the various subsidiaries of News Corp. and Hughes in the U.S., and developing and efficiently deploying innovations, such as next-generation set-top boxes with upgraded interactive television and digital video recorder capabilities and state-of-the-art anti-piracy techniques. When Hughes becomes part of News Corp.'s global family of DTH affiliates, it will benefit from a number of scale economies that will more efficiently defray the enormous research and development costs associated with bringing new features and services to market. Moreover, common technology standards for both hardware and software across the News Corp. DTH platforms should help to drive down consumer equipment and software costs. Through these various cost savings, DIRECTV will be able to finance more innovations in programming and technology to ensure that it achieves and maintains the highest level of service for its customers at competitive prices.

News Corp. also plans to bring to DIRECTV the "best practices" it has developed at its satellite operations in other countries. DIRECTV's "churn rate" – that is, the rate at which customers discontinue use of the service – is around 18 percent, whereas BSKyB's annual churn rate is currently 9.4 percent. By using BSKyB's "best practices" and accelerating the pace of innovation, we predict that DIRECTV should experience a 2 to 3 percent decline in its annual churn rate. We calculate that every percentage point reduction in churn will add approximately \$33 million to Hughes' earnings. With these additional financial resources, DIRECTV will be able to finance additional initiatives in research, development and marketing.

Another important element that News Corp. will bring to Hughes and DIRECTV is its deep and proven commitment to equal opportunity and diversity. Specifically, the diversity initiatives we will implement include:

- A commitment to carry more programming on DIRECTV targeted at culturally, ethnically and linguistically diverse audiences;

- An extensive training program for minority entrepreneurs seeking to develop program channels for carriage by multichannel video systems;
- A program for actively hiring and promoting minorities for management positions;
- An extensive internship programming for high school and college students;
- Improved procurement practices that ensure outreach and opportunities for minority vendors; and
- Upgraded internal and external communications, including the Hughes web site, to assist implementation of the above initiatives.

Finally, to my third point: there are no horizontal or vertical merger concerns arising from this transaction. Because this transaction involves an investment in DIRECTV, a multichannel video programming distributor with no programming interests, by News Corp., a programmer with no multichannel distribution interests, no "horizontal" competition issues arise. There will be no decrease in the number of U.S. competitors in either the multichannel video distribution market or the programming market. To the contrary, because of News Corp.'s plans to bring "best practices" and innovations to DIRECTV, competition in these markets will intensify and consumers will be presented with more and better choices.

The transaction does result in a "vertical" integration of assets because of the association of DIRECTV's distribution platform and News Corp.'s programming assets. But this "vertical" integration is not anti-competitive for two reasons. First, neither News Corp. nor DIRECTV has sufficient power in its relevant market to be able to act in an anti-competitive manner. DIRECTV has a modest 12 percent of the national multichannel market, compared to as much as 29 percent of the market held by the largest cable operator. News Corp. has a modest 3.9 percent of the national programming channels, compared to the largest cable programmer at 15.2 percent of the channels.

Second, rational business behavior will prevent News Corp. and DIRECTV from engaging in anti-competitive behavior. As a programmer, News Corp.'s business model is predicated on achieving the widest possible distribution for our programming in order to maximize advertising revenue and subscriber fees. Any diminution in distribution reduces our ability to maximize profit from that programming. Even if we were voluntarily willing to lower our earnings potential by withholding our programming from competing distributors, we would be precluded from doing so by the FCC's program access rules. Similarly, DIRECTV has every economic incentive to

draw from the widest spectrum of attractive programming, regardless of source, in order to maximize subscriber revenue. In short, it makes no business sense for either party to do anything to limit our potential customer base or our programming possibilities.

Notwithstanding these strong economic and business incentives, News Corp. and Hughes have agreed – as a matter of contract – to a series of program access undertakings to eliminate any concerns over the competitive effects of the proposed transaction. We have asked the FCC to adopt these program access commitments, which are attached to my written testimony, as a condition of the approval of our Application for Transfer of Control that was filed at the FCC on May 2. These program access commitments are largely the same as those required of cable operators, but in some respects go further. These commitments will:

- Prevent DIRECTV from discriminating against unaffiliated programmers;
- Prevent DIRECTV from entering into an exclusive arrangement with any affiliated programmer, including News Corp.; and
- Prevent News Corp. from offering any national or regional cable programming channels it controls on an exclusive basis to *any* distributor and from discriminating among distributors in price, terms or conditions.

These extensive commitments apply for as long as the FCC's program access rules remain in effect and News Corp. owns an interest in DIRECTV. They make it clear that News Corp. and Hughes are committed to fair, open and non-discriminatory program access practices that go well beyond what the law requires of DBS operators, cable programmers, and even cable operators.

In any event, neither News Corp. nor Hughes is among the top five media companies, by expenditure, in the United States. As you can see in the chart attached to my testimony, News Corp. is sixth with 2.8 percent of total industry expenditures, and Hughes is eighth with 2.2 percent. Even combining the expenditures of News Corp. and Hughes would place the company fifth in expenditures behind AOL Time Warner with 10.1 percent, Viacom with 6.4 percent, Comcast with 6.3 percent, and Sony at 5.3 percent. If the expenditures from Disney's theme parks were included in its total, the combination of News Corp. and Hughes would rank sixth in total "entertainment" revenues.

In closing, I believe this transaction represents an exciting association between two companies with the assets, experience and history of innovation that will ensure DIRECTV can become an even more effective competitor in the multichannel market. There will be significant public interest benefits for consumers as a result of this transaction, including bringing more local channels to more markets, innovations such as set-top boxes with next generation interactive television and digital video recorder capabilities, and a diversity program that will set the standard for the rest of the entertainment industry.

Thank you for your attention, and I look forward to your questions.

## EXHIBIT F

Program Access Requirements:  
News Corp. and DIRECTV Commitments

News Corp. and DIRECTV will be bound by the FCC's program access rules (otherwise applicable to vertically-integrated satellite cable programming services) regardless of whether News Corp., DIRECTV or any of their program services is deemed to be a vertically integrated satellite cable programming vendor under such rules.

In addition, News Corp. and DirecTV will make the following commitments, above and beyond those contained in the FCC's program access rules.

- News Corp. will not offer any of its existing or future national and regional programming services on an exclusive basis to any MVPD and will continue to make such services available to all MVPDs on a non-exclusive basis and non-discriminatory terms and conditions.
- Neither News Corp. nor DIRECTV will discriminate against unaffiliated programming services in the selection, price, terms or conditions of carriage.
- DIRECTV will not enter into an exclusive distribution arrangement with any Affiliated Program Rights Holder. "Affiliated Program Rights Holder" includes (i) a program rights holder in which News Corp. or DIRECTV holds a non-controlling "Attributable Interest" (as determined by the FCC's program access attribution rules); and (ii) a program rights holder in which an entity holding a non-controlling Attributable Interest in News Corp. or DIRECTV holds an Attributable Interest, provided that News Corp. or DIRECTV has actual knowledge of such entity's Attributable Interest in such program rights holder.

Liberty Media owns approximately 18% of the non-voting equity of News Corp. Liberty Media currently is considered a vertically integrated programmer under the FCC's program access rules and, as such, is restricted in its ability to enter into exclusive or discriminatory agreements with respect to satellite-delivered cable programming services in which it has an Attributable Interest. In the event Liberty Media is no longer deemed a vertically integrated programmer (including by reason of the sale of its Puerto Rican cable interests) and so long as Liberty Media holds an Attributable Interest in News Corp., DIRECTV will deal with Liberty Media with respect to programming services it controls as if it continued as a vertically integrated programmer subject to the program access rules.


























DIRECTV may continue to compete for programming that is lawfully offered on an exclusive basis by an unaffiliated program rights holder (e.g., NFL Sunday Ticket).

- Neither News Corp. nor DIRECTV (including any entity over which either exercises control) shall unduly or improperly influence: (i) the decision of any Affiliated Program Rights Holder to sell programming to an unaffiliated MVPD; or (ii) the prices, terms and conditions of sale of programming by any Affiliated Program Rights Holder to an unaffiliated MVPD.

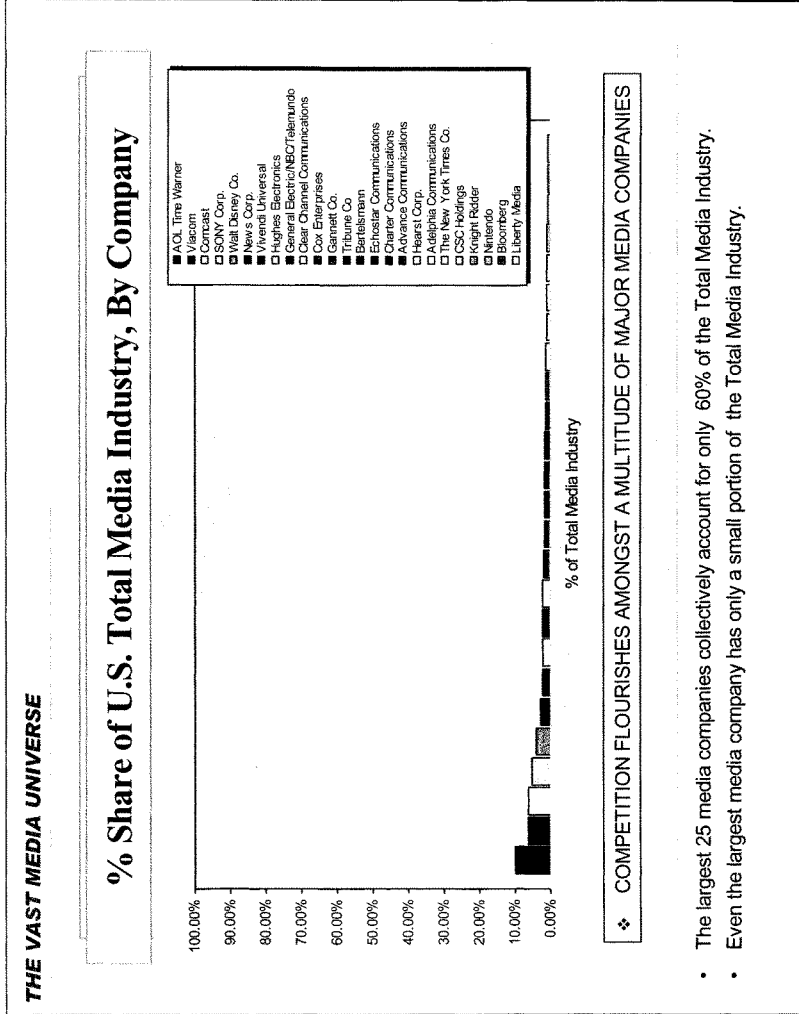
These commitments will apply to News Corp. and DIRECTV for the later of (1) as long as the FCC deems News Corp. to have an Attributable Interest in DIRECTV and the FCC's program access rules are in effect (provided that if the program access rules are modified these commitments shall be modified to conform to any revised rules adopted by the FCC) or (2) if these commitments are embodied in a consent decree or other appropriate order issued by or agreement with the DOJ, FTC or FCC, for the term specified by such consent decree, order or agreement.



**THE VAST MEDIA UNIVERSE****The U.S. Media Marketplace Is Highly Competitive**

	Company	2002 U.S. Media Revenues (in millions)	Company Revenues as a % of Total Media Industry
1	 AOL Time Warner	\$32,630	10.1%
2	 VIACOM	\$20,670	6.4%
3	 Comcast	\$20,470	6.3%
4	 SONY Corporation	\$17,090	5.3%
5	 The Walt Disney Co.	\$13,110	4.0%
6	 News Corporation	\$9,130	2.8%
7	 Vivendi Universal	\$7,580	2.3%
8	 Hughes Electronics	\$7,190	2.2%
9	 General Electric/NBC/Telemundo	\$7,150	2.2%
10	 Clear Channel Communications	\$6,920	2.1%
11	 Cox Enterprises	\$6,400	2.0%
12	 Gannett Co.	\$5,590	1.7%
13	 The Tribune Company	\$5,400	1.7%
14	 Bertelsmann	\$5,270	1.6%
15	 Echostar Communications	\$4,750	1.5%
16	 Charter Communications	\$4,570	1.4%
17	 Advance Publications	\$4,000	1.2%
18	 Hearst Corporation	\$3,990	1.2%
19	 Adelphia Communications	\$3,340	1.0%
20	 The New York Times Company	\$3,080	1.0%
21	 Cablevision Systems Corporation	\$3,070	0.9%
22	 Knight Ridder	\$2,840	0.9%
23	 Nintendo	\$2,130	0.7%
24	 Bloomberg	\$2,110	0.7%
25	 Liberty Media	\$2,080	0.6%
<b>Totals for the Top 25 Media Companies (By Revenue)</b>		<b>\$200,560</b>	<b>62.1%</b>

Source: Corporate SEC filings (except as noted in the End Notes).



**THE VAST MEDIA UNIVERSE****END NOTES**

1. Media include the following industry segments: broadcast television, broadcast radio, cable & satellite providers, cable & satellite programming, newspaper publishing, consumer magazine publishing, consumer book publishing, consumer Internet sites, filmed entertainment, recorded music, interactive entertainment, and outdoor advertising (the "Media"). Total U.S. expenditures (end-user spending) on the Media was estimated to be \$324.006 billion in 2002 (the "Total Media Industry"). *Source: PQ Media, LLC; Veronis Suhler Stevenson.* Company revenues for the Media are reported as a percentage of the Total Media Industry. Since most private companies do not publicly report financial performance, data on total revenues for the Media is unavailable. The Total Media Industry, which includes expenditures on both publicly- and privately-owned companies, approximates total U.S. revenue for both public and private companies operating in the Media.
2. Corporate SEC filings for AOL Time Warner, Comcast, News Corporation, CSC Holdings and Tribune Company do not separately break out revenues for certain segments (e.g., sports teams) that are not among the segments that comprise the Total Media Industry.
3. Corporate SEC filings for Viacom and Clear Channel Communications and Bertelsmann's Annual Report do not separately break out revenues for certain segments (e.g., theme parks, live entertainment and media services) that are not among the segments that comprise the Total Media Industry.
4. As reported in its 10-K, Comcast's figures include unaudited *pro forma* revenues for AT&T Broadband, which merged with Comcast in November 2002.
5. News Corp.'s figures include U.S. and Canadian revenues for both Fox Entertainment Group, Inc. and Harper Collins, but exclude revenues for the New York Post.
6. SONY, Vivendi Universal, Hughes Electronics, GE/NBC/Telemundo, CSC Holdings, Nintendo, and Liberty Media figures may include some non-U.S. revenues.
7. The figures for Cox Enterprises are 2001 revenues and have been derived from the company's web site, <http://www.coxenterprises.com>.
8. Adelphia Communications' figures are an estimate based on financial statements filed by the company with the United States Bankruptcy Court on November 25, 2002. See Mike Farrell, *Adelphia's Numbers Aren't All Bad*, Multichannel News, December 2, 2002, at 6.
9. Revenues for the following, privately-held companies have been derived from Advertising Age: Advance Publications, Hearst Corporation and Bloomberg. See *Leading Media Companies*, Advertising Age, August 19, 2002, at S-2. The revenue figures for these companies are 2001 figures and may exclude certain revenues from certain industry segments that comprise the definition of the Total Media Industry.

**Securities Laws Information**

In connection with the proposed transactions, General Motors Corporation ("GM"), Hughes Electronics Corporation ("Hughes") and The News Corporation Limited ("News") intend to file relevant materials with the Securities and Exchange Commission ("SEC"), including one or more registration statement(s) that contain a prospectus and proxy/consent solicitation statement. Because those documents will contain important information, investors and security holders are urged to read them, if and when they become available. When filed with the SEC, they will be available for free (along with any other documents and reports filed by GM, Hughes or News with the SEC) at the SEC's website, [www.sec.gov](http://www.sec.gov). GM stockholders will also receive information at an appropriate time on how to obtain transaction-related documents for free from GM. When these documents become available, News stockholders may obtain these documents free of charge by directing such request to: News America Incorporated, 1211 Avenue of the Americas, 7th Floor, New York, New York 10036, attention: Investor Relations.

GM and its directors and executive officers and Hughes and certain of its executive officers may be deemed to be participants in the solicitation of proxies or consents from the holders of GM \$1-2/3 common stock and GM Class H common stock in connection with the proposed transactions. Information about the directors and executive officers of GM and their ownership of GM stock is set forth in the proxy statement for GM's 2003 annual meeting of shareholders. Participants in GM's solicitation may also be deemed to include those persons whose interests in GM or Hughes are not described in the proxy statement for GM's 2003 annual meeting. Information regarding these persons and their interests in GM and/or Hughes was filed pursuant to Rule 425 with the SEC by each of GM and Hughes on April 10, 2003. Investors may obtain additional information regarding the interests of such participants by reading the prospectus and proxy/consent solicitation statement if and when it becomes available.

This communication shall not constitute an offer to sell or the solicitation of an offer to buy any securities, nor shall there be any sale of securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction. No offering of securities shall be made except by means of a prospectus meeting the requirements of Section 10 of the Securities Act of 1933, as amended.

Materials included in this document contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that could cause actual results to be materially different from historical results or from any future results expressed or implied by such forward-looking statements. The factors that could cause actual results of GM, Hughes and News to differ materially, many of which are beyond the control of GM, Hughes or News include, but are not limited to, the following: (1) operating costs, customer loss and business disruption, including, without limitation, difficulties in maintaining relationships with employees, customers, clients or suppliers, may be greater than expected following the transaction; (2) the regulatory approvals required for the transaction may not be obtained on the terms expected or on the anticipated schedule; (3) the effects of legislative and regulatory changes; (4) an inability to retain necessary authorizations from the FCC; (5) an increase in competition from cable as a result of digital cable or otherwise, direct broadcast satellite, other satellite system operators, and other providers of subscription television services; (6) the introduction of new technologies and competitors into the subscription television business; (7) changes in labor, programming, equipment and capital costs; (8) future acquisitions, strategic partnerships and divestitures; (9) general business and economic conditions; and (10) other risks described from time to time in periodic reports filed by GM, Hughes or News with the SEC. You are urged to consider statements that include the words "may," "will," "would," "could," "should," "believes," "estimates," "projects," "potential," "expects," "plans," "anticipates," "intends," "continues," "forecast," "designed," "goal," or the negative of those words or other comparable words to be uncertain and forward-looking. This cautionary statement applies to all forward-looking statements included in this document.